CLERK'S COPY.

TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1929

No. 128

THE UNITED STATES, PETITIONER

vs.

AMERICAN CAN COMPANY

No. 129

THE UNITED STATES, PETITIONER

vs.

MISSOURI CAN COMPANY

No. 130

THE UNITED STATES, PETITIONER

vs.

DETROIT CAN COMPANY

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR CERTIORARI FILED JUNE 4, 1929
CERTIORARI GRANTED OCTOBER 14, 1929

(34259)
(34260)
(34261)



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1 In United States District Court

District of New Jersey

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Docket Entries

Jan. 22, 1926. Petition filed.
Jan. 22, 1926. Affidavit of service filed.
April 28, 1926. Answer filed.
August 2, 1926. Notice of trial filed.
September 4, 1926. Notice of trial filed.
January 13, 1927. Trial. Adjourned to day to be fixed.
May 16, 1927. Trial. Adjourned to May 24, 1927.
May 24, 1927. Trial. Decision reserved.
May 31, 1927. Memorandum filed.
June 11, 1927. Defendant's request for findings of fact filed.
June 11, 1927. Motion for judgment for defendant filed.
August 16, 1927. Findings of fact and conclusions of law filed.
August 16, 1927. Rule for judgment final for plaintiff for $3,953,-892.39 filed.
September 17, 1927. Order extending term filed.
October 11, 1927. Order extending term filed.
November 9, 1927. Bill of exceptions filed.
2 November 9, 1927. Assignment of errors filed.
November 9, 1927. Petition for writ of error filed.
November 9, 1927. Order allowing writ of error filed.
November 9, 1927. Writ of error issued.
November 9, 1927. Citation issued.
November 15, 1927. Citation returned, service acknowledged. Copy filed.
November 18, 1927. Order for leave to withdraw files for printing filed.

In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Petition

Filed January 22, 1926

To the Honorable Judges of the United States District Court for the District of New Jersey.

The petition of American Can Company, the above-named plaintiff, respectfully shows:—

1. The plaintiff was, during all the times hereinafter
3 mentioned, and now is, a corporation duly organized and existing under the laws of the State of New Jersey, having its legal residence and its principal office in the State of New Jersey, at Jersey City, Hudson County, in the District of New Jersey, and engaged in the business of manufacturing and selling cans and other containers, having its principal business office in the borough of Manhattan, city, county and State of New York, and in the Southern District of New York.

2. On information and belief, that during all the times hereinafter mentioned up to March, 1921, one William H. Edwards was the collector of internal revenue of the United States for the Second District of New York, the district in which the plaintiff had and now has its principal place of business; that said Edwards is not now in office as collector of internal revenue of the United States for said district; and that one Frank K. Bowers, since March, 1921, has been and now is the collector of internal revenue of the United States for said district.

3. The plaintiff and its subsidiary companies, to wit, the Missouri Can Company, the Detroit Can Company, the American Can Co., of Massachusetts, the American Can Company of Utah, the Sanitary Can Company, the Chas. W. Shonk Co., the Union Can Company, the Davenport Can Company, the Newton Manufacturing Co., the Wade Machine Company, the Raleigh Manufacturing Co., and the Newbern Box Company, corporations of which the plaintiff owned all the capital stock, kept their accounts during 1917 upon the basis of accruing their receipts and disbursements, valuing the normal stocks of tin plate carried in their inventories at a constant figure regardless of changes in the cost or market value of tin plate and valuing the other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased. The plaintiff, the Missouri Can Company, the Detroit Can Company,
4 the American Can Company of Massachusetts, the American Can Company of Utah, and the Sanitary Can Company, carried in their inventories large stocks of tin plate, and tin plate was the principal, and by far the most important, material used by the plaintiff and said companies in their business of manufacturing cans and other containers, the value of their stocks of tin plate being approximately one-half the total value of all the materials carried in their inventories. The plaintiff and all its said subsidiary companies determined their incomes and duly made and filed with said Edwards, as such collector of internal revenue, their income and excess profits tax returns for 1917 upon the basis upon which their accounts were kept. The amount of the net income of the plaintiff as so determined and returned was $16,927,404.35 (including $60,010.50 as dividends), and the amount of the

consolidated net income of the plaintiff and its said subsidiary companies as so determined and returned was $17,994,400.46 (including $60,010.50 as dividends). The amount of the consolidated invested capital of the plaintiff and its said subsidiary companies as so returned was $97,019,377.66. On or about June 14, 1918, the plaintiff paid, and the said Edwards, as such collector of internal revenue, collected from the plaintiff $3,266,499.86 as and for the total excess profits tax for 1917 payable by the plaintiff and its said subsidiary companies and the income tax for 1917 payable by the plaintiff in accordance with said returns. The subsidiary companies hereinabove mentioned were the only corporations organized in the United States and the only domestic corporations of which the plaintiff owned or controlled all or substantially all the stock in or during 1917. On information and belief that there were no interests which owned substantially all the stock of the plaintiff and any other corporation in or during 1917.

4. Thereafter and prior to September 21, 1920, the Commissioner of Internal Revenue, through his representatives, examined said returns and the books and records of the plaintiff and its said subsidiary companies and objected to certain items affecting the income and invested capital of the plaintiff and made certain adjustments which had the effect of increasing the net income of the plaintiff to $18,211,125.72 (including $60,010.50 as dividends) and the consolidated net income of the plaintiff and its said subsidiary companies to $19,278,121.83 (including $60,010.50 as dividends) and reducing the consolidated invested capital of the plaintiff and its said subsidiary companies to $60,343,799.18, but did not affect the basis on which the plaintiff and its said subsidiary companies had kept their accounts and valued their inventories during 1917. On information and belief that thereafter and prior to September 21, 1920, the Commissioner of Internal Revenue, in accordance with said adjustments, made assessments against the plaintiff for additional income and excess profits taxes for 1917 aggregating $1,953,480.79. The plaintiff paid and said Edwards, as such collector of internal revenue, collected from the plaintiff $520,762.54 on or about November 22, 1919, and $1,432,718.25 on or about September 21, 1920, as and for such additional income and excess profits taxes for 1917.

5. Thereafter, the Commissioner of Internal Revenue, through his representatives, examined further the books and records of the plaintiff and its said subsidiary companies and objected to the basis upon which the plaintiff and its said subsidiary companies had valued their inventories of tin plate and determined their net incomes for 1917, and on or about March 7, 1921, the Commissioner of Internal Revenue issued and mailed a letter to the plaintiff, of which a copy is hereto attached and made a part hereof marked "Exhibit A," in which he stated in substance that the basis upon which the plaintiff

and its said subsidiary companies had valued their inventories
6 of tin plate and determined their net incomes for 1917 was not
correct, undertook to revalue their inventories of tin plate, and redetermine their net incomes upon a different basis and made adjustments which had the effect of increasing the net income of the plaintiff to $22,933,625.72 (including $60,010.50 as dividends) and the consolidated net income of the plaintiff and its said subsidiary companies to $24,949,688.51 (including $60,010.50 as dividends) and had the effect of increasing the consolidated invested capital of the plaintiff and its said subsidiary companies to $60,348,919.50. On information and belief, that thereafter the Commissioner of Internal Revenue, in accordance with said adjustments, made an assessment against the plaintiff for additional income and excess-profits taxes for 1917 amounting to $3,383,481.46.

6. On or about December 5, 1921, the plaintiff filed with said Bowers, as such collector of internal revenue, a claim for the abatement of the full amount of said assessment, amounting to $3,383,481.46, and on or about December 14, 1922, the plaintiff duly made and filed with said Bowers, as such collector, according to the provisions of law in that regard and the regulations of the Secretary of the Treasury established in pursuance thereof, a claim for the refund of income and excess-profits taxes for 1917 amounting to $3,343,139.35, which were included in the taxes which the plaintiff had paid on June 14, 1918, November 22, 1919, and September 21, 1920, as hereinabove stated. Said claim for refund was made out in the form prescribed by said regulations and all the facts relied upon in support of said claim were clearly set forth under oath. It was stated in said claim, among other things, that the Commissioner of Internal Revenue had determined that the basis upon which the taxpayer had kept its accounts and made its returns for 1917 did not clearly reflect the net income and had calculated the net income on a different basis and assessed additional taxes amounting to $3,383,481.46 as the
result thereof; that if the basis on which the taxpayer had
7 kept its accounts did not clearly reflect its net income, the taxes
should be computed on the basis of actual receipts and disbursements; that the amount of the plaintiff's net income for 1917 calculated upon the basis of actual receipts and disbursements was $10,772,615.01; that the amount of the consolidated net income of the plaintiff and its said subsidiary companies for 1917, calculated upon said basis, was $11,403,785.85; that the correct amount of the income and excess-profits taxes for 1917 payable by the plaintiff was $1,876,841.30; that the plaintiff had already paid as and for such taxes $5,219,980.65; that the taxes so paid by the plaintiff were in excess of those properly collectible by $3,343,139.35; and that the amount of such excess should be refunded. On information and belief that on or after January 26, 1924, the Commissioner of Internal Revenue disallowed and rejected said claim for abatement and said claim for refund. Thereafter, the plaintiff paid to said Bowers, as such col-

lector of internal revenue, under protest, the amount of the assessment involved in said claim for abatement with interest, and duly brought an action against said Bowers in the District Court of the United States for the Southern District of New York to recover back the amount so paid. Said action is still pending undetermined.

7. The plaintiff has recently made a more careful and detailed calculation of its net income and that of its said subsidiary companies upon the basis of actual receipts and disbursements. On information and belief that the amount of the net income of the plaintiff for 1917 determined upon the basis of actual receipts and disbursements as defined in section 12 (a) of the revenue act of 1916, approved September 8, 1916, as amended by the revenue act of 1917 approved October 3, 1917—that is to say, by deducting from the gross amount of the income received in 1917 the amounts of (1) the ordinary and
8 necessary expenses paid in 1917 in the maintenance and operation of the business and properties, (2) the losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise, subject to the limitations contained in paragraph second of said section 12 (a); (3) the interest on indebtedness paid in 1917 (except on indebtedness incurred for the purchase of obligations or securities, the interest upon which was exempt from taxation as income under said act) subject to the limitations contained in paragraph third of said section 12 (a), and (4) the taxes paid in 1917 imposed by the authority of the United States (except income and excess-profits taxes), or of its Territories, or possessions, or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits, was not more than $12,783,418.91 (including $60,010.50 as dividends); that the amount of the consolidated net income of the plaintiff and its said subsidiary companies for 1917 determined on said basis was not more than $13,297,216.86 (including $60,010.50 as dividends); that the correct amount of the excess-profits taxes for 1917 payable by the plaintiff and its said subsidiary companies and the income taxes for 1917 payable by the plaintiff in accordance with the revenue acts applicable thereto was not more than $2,537,958.32; and that the plaintiff has paid, and the said Edwards as such collector of internal revenue has collected from the plaintiff, as and for such taxes, at least $2,681,702.74 in excess of the amount properly due and payable.

8. On information and belief that the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, made regulations which provided that all materials carried in inventories should be valued on the basis of (a) cost or (b) cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased, and that the basis upon which the plaintiff and its said subsidiary companies kept their accounts and made their returns for 1917 was not in accordance with said regulations. On information and belief that the Commis-

sioner of Internal Revenue ruled and determined that the basis upon which the plaintiff and its said subsidiary companies valued their inventories of tin plate and determined their net incomes for 1917 did not clearly reflect their incomes and was not authorized or permitted by the revenue acts applicable to 1917 or the regulations made thereunder, that their incomes for 1917 should not be determined upon the basis upon which they kept their accounts and made their returns and their income and excess-profits taxes for 1917 should not be computed upon their incomes as returned. The plaintiff claims that the net incomes of the plaintiff and its said subsidiary companies for 1917 should be determined upon the basis of actual receipts and disbursements as defined in section 12 (a) of the revenue act of 1916, as amended by the revenue act of 1917, and that their income and excess-profits taxes for 1917 should be computed upon their net incomes as so determined. There have been erroneously and illegally assessed against and collected from the plaintiff internal revenue taxes, to wit, income and excess-profits taxes for 1917, amounting to at least $2,681,702.74, and that the plaintiff has paid to said Edwards as such collector of internal revenue as and for income and excess-profits taxes for 1917, the sum of at least $2,681,702.74, which was excessive and wrongfully collected. The said sum of $2,681,702.74, with interest at the rate of six per cent (6%) per annum, on $728,221.95 from June 14, 1918; on $520,762.54 from November 22, 1919; and on $1,432,718.25 from September 21, 1920, is the sum of money or other thing claimed and the damages sought to be recovered by the plaintiff in this suit.

Wherefore, the plaintiff prays judgment upon the facts and law and demands judgment against the defendant for the sum of
10 $2,681,702.74 with interest at the rate of six per cent (6%) per annum on $728,221.95 from June 14, 1918; on $520,762.54 from November 22, 1919; and on $1,432,718.25 from September 21, 1920, together with the costs of this suit.

JOHN J. TREACY,
Attorney for Plaintiff.

Office and post-office address, 1 Exchange Place, Jersey City, N. J.

[*Duly sworn to by Henry W. Phelps; jurat omitted in printing.*]

12 *Exhibit A to petition*

TREASURY DEPARTMENT,
Washington, March 7, 1921.

[Office of Commissioner of Internal Revenue. Address reply to Commissioner of Internal Revenue and refer to IT:SA:CR:TA—JAC]

AMERICAN CAN COMPANY OF NEW JERSEY,
120 Broadway, New York, N. Y.

SIRS: An examination of the income and consolidated excess profits tax returns for the calendar year 1917, filed by you and your affiliated

companies, has been made in this office in connection with a field investigation completed January 17, 1921, and an additional tax amounting to $3,383,481.46 found due from you.

The adjustments resulting in this additional tax are explained in the accompanying Schedules 1 to 31, inclusive.

The excess-profits tax for 1917 has been allocated in accordance with your instructions.

The collector of internal revenue for your district will notify you as to the time and manner of making payment of this additional tax.

Respectfully,

G. V. NEWTON,
Deputy Commissioner.

Enclosures: Schedules 1 to 31, inc.

13 American Can Company, year ended December 31, 1917

Schedule 1.—Income adjustments (American Can Company)

Net income as amended by department	$18,211,125.72
As corrected	22,933,625.72
Increased as explained below	4,722,500.00
Increases:	
(a) Cost of goods sold	4,722,500.00

Reasons for changes

(a) This item represents a charge to costs of raw material put in process over the actual cost at which same was inventoried at December 31, 1916. The credit was placed to "Inventory constant" account. The entry was made in anticipation of a drop in the market at some future date, when a loss would occur on account of high-priced inventories at hand.

For income-tax purposes, all income must be returned in the year in which realized, and if the market should slump at a future date the loss would be taken in the year in which realized.

The entry referred to above would result in an elimination of profits realized through rise in market values, and therefore has been disallowed.

14 American Can Company, year ended December 31, 1917

Schedule 2.—Income adjustments (Missouri Can Company)

Net income as reported on original return	$253,559.18
As corrected	422,059.18
Increase as explained below	168,500.00
Increases:	
(a) Cost of goods sold	168,500.00

Reasons for changes

(a) Cost of goods sold, $168,500.00. (For explanation, see Schedule 1.)

Schedule 3.—Income adjustments (Detroit Can Company)

Net income as reported on original return	$104,786.64
As corrected	174,786.64
Increase as explained below	70,000.00
Increases:	
(a) Cost of goods sold	70,000.00

Reasons for changes

(a) Cost of goods sold $70,000.00. (For explanation see Schedule 1.)

15 American Can Company, year ended December 31, 1917

Schedule 4.—Income adjustments (American Can Co. of Massachusetts)

Net income as reported on original return	$313,885.48
As corrected	505,385.48
Increase as explained below	191,500.00
Increases:	
(a) Cost of goods sold	191,500.00

Reasons for changes

(a) Cost of goods sold $191,500.00. For explanation, see Schedule 1.

Schedule 5.—Income adjustments (American Can Company of Utah)

Net income as reported on original return	$133,007.24
As corrected	184,007.24
Increase as explained below	51,000.00
Increases:	
(a) Cost of goods sold	51,000.00

Reasons for changes

(a) Cost of goods sold $51,000.00. (For explanation, see Schedule 1.)

16 American Can Company, year ended December 31, 1917

Schedule 6.—Income adjustments. (*Sanitary Can Company*)

Net income as reported on original return	$8,330.14
As corrected	471,330.14
Increase as explained below	463,000.00
Increases:	
(a) Cost of goods sold	463,000.00

Reasons for changes

(a) Cost of goods sold $463,000.00. (For example, see Schedule 1.)

Schedule 7.—Income adjustments. (*Chas. W. Shonk Co.*)

Net income as reported on original return	$269,024.23
As corrected	269,024.23
Increase	None.

Schedule 8.—Income adjustments. (*Union Can Company*)

Loss as reported on original return	$8,706.17
As corrected—loss	3,706.17
Increase as explained below	5,000.00
Increases:	
(a) Cost of goods sold	5,000.00

Reasons for changes

(a) Cost of goods sold $5,000.00. (For explanation, see Schedule 1.)

17 American Can Company, year ended December 31, 1917

Schedule 9.—Income adjustments. (*Davenport Can Company*)

Loss as reported on original return	$4,430.48
As corrected—loss	4,383.80
Increase as explained below	46.68
Increases:	
(a) Contingent fund addition	46.68

Reasons for changes

(a) Contingent fund addition, $46.68.

Reserves set aside for contingent funds can not be deducted in income tax returns.

Schedule 10.—Income adjustments. (*Newton Manufacturing Co.*)

Net loss as reported on original return	$1,127.57
As corrected	1,127.57
Increase	None.

18 *Schedule 11.—Income adjustments* (*Wade Machine Company*)

Net loss as reported on original return	$1,332.56
As corrected, net loss	1,332.56
Decrease	None.

American Can Company, year ended December 31, 1917

Schedule 12.—Income adjustments (*Raleigh Manufacturing Co.*)

Net income as reported on return	None.
As corrected	None.
Increase	None.

Schedule 13.—Income adjustments (*Newbern Box Company*)

Net income as reported on original return	None.
As corrected	None.
Decrease	None.

19 American Can Company, year ended December 31, 1917

Schedule 14.—Consolidated Net Income, 1917

Net income as corrected:		
American Can Company	$22,933,625.72	
Missouri Can Company	422,059.18	
Detroit Can Company	174,786.64	
American Can Company of Massachusetts	505,385.46	
American Can Company of Utah	184,007.24	
Sanitary Can Company	471,330.14	
Chas. W. Shonk Company	269,024.23	
Total		$24,960,218.61
Net losses as corrected:		
Union Can Company	$3,706.17	
Davenport Can Company	4,383.80	
Newton Manufacturing Co	1,127.57	
Wade Machine Company	1,332.56	
Total		10,550.10
Aggregate net income		24,949,668.51
Deduct:		
Dividends received by American Can Company from domestic corporations		60,010.50
Consolidated net income for excess profits tax purposes		24,889,658.01

20 American Can Company, year ended December 31, 1917

Schedule 15.—Consolidated invested capital, 1917

As amended by department July 5, 1919		$60,343,799.18
As corrected		60,348,919.50
Increase as explained below		5,120.32
Increases:		
(a) American Can Co., income tax reserve	$3,011.16	
(b) Shonk Company, income tax reserve	2,109.16	
		5,120.32

Reasons for changes

(a) This item represents reserve for income tax and may be included as a part of invested capital.

Balance shown on books	$162,453.52
Amount used in previous adj	159,442.36
Difference	3,011.16

(b) This item represents reserve for income tax and may be included as a part of invested capital.

21 American Can Company, year ended December 31, 1917

Schedule 16.—Computation of excess-profits tax

Consolidated invested capital (Schedule 15)		$60,348,919.50
Consolidated net income (Schedule 14)		24,889,658.01
Deduction:	Income	Tax
9%, $5,431,402.76, plus $3,000.00	$5,434,402.76	
Taxable at 20%	$3,617,935.17	$723,587.03
25%	3,017,445.98	754,361.50
35%	3,017,445.98	1,056,106.09
45%	4,827,913.56	2,172,561.10
60%	4,974,514.56	2,984,708.74
	$24,889,658.01	$7,691,324.46

Schedule 17.—Allocation of excess-profits tax

Name of company	Per cent	Amount
American Can Company	100%	$7,691,324.46

22 American Can Company, year ended December 31, 1917

Schedule 18.—Computation of total tax, 1917 (American Can Company)

Net income (Schedule 1)	$22,933,625.72	
Deduct: Excess-profits tax (Schedule 17)	7,691,324.46	
		Tax
Taxable at 2%	$15,242,301.26	$304,846.02
Less dividends from 1916 and 1917 earnings	60,010.50	
Taxable at 4%	$15,182,290.76	607,291.63
Excess-profits tax as above		7,691,324.46
Total tax		$8,603,462.11
Previously assessed		5,219,980.65
Additional tax to be assessed		$3,383,481.46

Schedule 19.—Computation of total tax, 1917 (Missouri Can Company)

Net income (Schedule 2)	$422,059.18	
Deduct: Excess-profits tax	None.	
		Tax
Taxable at 2%	$422,059.18	$8,441.18
Taxable at 4%	$422,059.18	16,882.36
Total tax		$25,323.54
Previously assessed		15,213.54
Additional tax to be assessed		$10,110.00

23 American Can Company, year ended December 31, 1917

Schedule 20.—Computation of total tax, 1917 (Detroit Can Company)

Net income (Schedule 3)	$174,786.64	
Deduct: Excess-profits tax	None.	
		Tax
Taxable at 2%	$174,786.64	$3,495.73
Taxable at 4%	$174,786.64	6,991.46
Total tax		$10,487.19
Previously assessed		6,287.19
Additional tax to be assessed		$4,200.00

Schedule 21.—Computation of total tax, 1917 (American Can Company of Mass.)

Net income (Schedule 4)	$505,385.46	
Deduct: Excess-profits tax	None.	
Taxable at 2%	$505,385.46	$10,107.71
Taxable at 4%	$505,385.46	20,215.42
Total tax		$30,323.13
Previously assessed		18,833.13
Additional tax to be assessed		$11,490.00

24 American Can Company, year ended December 31, 1917

Schedule 22.—Computation of total tax, 1917 (American Can Company of Utah)

Net income (Schedule 5)	$184,007.24	
Deduct: Excess-profits tax	None.	
		Tax
Taxable at 2%	$184,007.24	$3,680.14
Taxable at 4%	184,007.24	7,360.28
Total tax		$11,040.42
Previously assessed		7,980.42
Additional tax to be assessed		$3,060.00

Schedule 23.—Computation of total tax, 1917 (Sanitary Can Company)

Net income (Schedule 6)	$471,330.14	
Deduct: Excess-profits tax	None.	
		Tax
Taxable at 2%	$471,330.14	$9,426.60
Taxable at 4%	$471,330.14	18,853.20
Total tax		$28,279.80
Previously assessed		499.80
Additional tax to be assessed		$27,780.00

25 American Can Company, year ended December 31, 1917

Schedule 24.—Computation of total tax, 1917 (Chas. W. Shonk Company)

Net income (Schedule 7)	$269,024.23	
Deduct: Excess-profits tax	None.	
		Tax
Taxable at 2%	$269,024.23	$5,380.48
Taxable at 4%	$269,024.23	10,760.97
Total tax		$16,141.45
Previously assessed		16,141.45
Additional tax to be assessed		None.

Schedule 25.—Computation of total tax, 1917 (Union Can Company)

Net loss (Schedule 8)	$3,706.17	
		Tax
Total tax		None.
Previously assessed		None.
Additional tax to be assessed		None.

26 American Can Company, year ended December 31, 1917

Schedule 26.—Computation of total tax, 1917 (Davenport Can Company)

Net loss (Schedule 9)	$4,383.80	
		Tax
Total tax		None.
Previously assessed		None.
Additional tax to be assessed		None.

Schedule 27.—Computation of total tax, 1917 (Newton Manufacturing Co.)

Net loss (Schedule 10)	$1,127.57	
		Tax
Total tax		None.
Previously assessed		None.
Additional tax to be assessed		None.

Schedule 28.—Computation of total tax, 1917 (Wade Machine Company)

Net loss (Schedule 11)	$1,332.56	
		Tax
Total tax		None.
Previously assessed		None.
Additional tax to be assessed		None.

American Can Company, year ended December 31, 1917

Schedule 29.—Computation of total tax, 1917 (Raleigh Manufacturing Co.)

Net income (Schedule 12)	None.
Total tax	None.
Previously assessed	None.
Additional tax to be assessed	None.

Schedule 30.—Computation of total tax, 1917 (Newbern Box Company)

Net income (Schedule 13)	None.
Total tax	None.
Previously assessed	None.
Additional tax to be assessed	None.

Schedule 31.—Summary of additional tax

American Can Co., parent	$3,383,481.46
Missouri Can Co	10,110.00
Detroit Can Co	4,200.00
American Can Co. of Mass	11,490.00
American Can Co. of Utah	3,060.00
Sanitary Can Co	27,780.00
Total	$3,440,121.46

28 In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Affidavit of service

Filed Jan. 22, 1926

STATE OF NEW JERSEY,
County of Mercer, ss:

John J. Treacy, being duly sworn, deposes and says:

I am the attorney for the plaintiff in the above-entitled suit. On the 22nd day of January, 1926, I filed the original petition in said suit with the clerk of the United States District Court for the District of New Jersey. I served a copy of said petition upon the district attorney of the United States for said district, and I mailed a copy of said petition, by registered letter, to the Attorney General for the United States, all as provided in sections 5 and 6 of the act of Congress approved March 3, 1887, commonly known as the "Tucker Act."

JOHN J. TREACY.

Subscribed and sworn to before me this 22nd day of January, 1926.

R. S. CHEVRIER,
Deputy Clerk.

29 In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF
vs.
THE UNITED STATES, DEFENDANT
} On petition, etc.

Answer

Filed April 28, 1926

Defendant, United States of America, appearing herein by Walter G. Winne, United States Attorney for the District of New Jersey, answering, says:

1. It admits the allegations contained in paragraphs 1, 2, 4, 5, and 6 of the petition.

2. It has no knowledge as to the allegations contained in paragraph 3 of the petition.

3. Defendant has no knowledge or information sufficient to form a belief as to the allegations contained in paragraph 7 relative to the calculations made by plaintiff. It denies that there was collected from plaintiff anything in excess of the amount properly due and payable.

4. As to the allegations contained in paragraph 8, defendant admits the making of the regulations by the Commissioner of Internal Revenue and his rulings and determinations, but denies that the assessment and collection of the taxes was erroneous and illegal.

WALTER G. WINNE,
United States Attorney,
Attorney for Defendant.

30 In United States District Court

AMERICAN CAN COMPANY, MISSOURI CAN COMPANY, AND DETROIT CAN COMPANY, plaintiffs

vs.

THE UNITED STATES, DEFENDANT

Bill of exceptions

Filed Nov. 9, 1927

Transcript of proceedings taken at Trenton, N. J., before Hon. JOSEPH L. BODINE, D. J., January 13, 1927.

Appearances of counsel

John J. Treacy, Esq., Graham Sumner, Esq., for the plaintiffs; Walter G. Winne, Esq., U. S. attorney, Walter H. Bacon, jr., Esq., assistant United States attorney, Charles T. Hendler, Esq., special attorney, Internal Revenue, for the Government.

31 *Colloquy between court and counsel*

Mr. SUMNER. There are three cases here, your honor, one is the American Can Company, the parent company, and two of the subsidiary companies, and all the evidence that would be introduced in the American Can Company case would include practically all of the evidence that would be needed in the other cases, and it seems it would be a convenience if we could make a stipulation to the effect that the three cases be tried together.

The COURT. There is no objection to that, is there?

Mr. HENDLER. The only thing that occurs to me in regard to that is this: There may be a variation in facts that might lead to some confusion if they went along altogether that way.

The COURT. But there is no danger. You cannot confuse the mind of the court.

Mr. HENDLER. It might be somewhat difficult for even the lawyers to carry along the facts of the purchases and sales of the three different corporations at one time. That is the only thing I have in mind.

The COURT. Let us take it, and see how we get along.

Mr. SUMNER. Of course, it will be necessary to have three separate decisions and separate records and all that, but it would perhaps eliminate repetition if we could stipulate that whatever was taken in this main case should apply to the other two cases.

The COURT. Suppose we enter an order now consolidating the three cases for the purpose of trial. Now, we will have the record, so it seems to me that from that record if we do become confused it will be perfectly easy to segregate the evidence. Now, may I have all your witnesses sworn at once?

Mr. SUMNER. Would your honor like me to make a statement as to the nature of these cases?

The COURT. Yes.

Mr. SUMNER. There are certain questions of law about the
32 interpretation of the revenue act of 1917, and the only question of fact to amount to anything is the determination of the income of these corporations on the cash basis as distinguished from the accrual basis.

I will hand to your honor a brief which I have prepared for your convenience, as it has extracts from the statute in reference to some of the authorities. I will hand a copy to the other side, although it is not, of course, an exhaustive or complete brief on the law.

The American Can Company is the parent company and it had in 1917 twelve subsidiary companies. They were all engaged in the business of manufacturing and selling cans and other containers and also the manufacture of munitions for the United States and other governments. And they kept their accounts during 1917 on what is called the accrual basis, on which they treated accounts receivable

as equivalent of receipts and accounts payable as equivalent of disbursements, and they valued their inventory on the basis of cost or market value, whichever was lower, except for their normal stocks of tin plate which they valued at a constant figure, irrespective of change in market value.

They made their income and excess profit tax return for 1917 on the basis on which they kept their accounts. Their returns were filed in 1918, and in June, 1918, they made payments to the collector of internal revenue in New York City, of the amounts of the income and excess profits taxes, which were payable in accordance with the figures stated in their returns. I will not trouble your honor with all the figures now, as I think it would just complicate the point. After the filing of these returns and prior to March 7, 1921, the Commissioner of Internal Revenue examined all the books and records of these corporations to check up their returns for 1917, and he made certain changes in both the invested capital and the income which had the effect of increasing the taxes to a considerable extent. That is, he increased the income and he reduced the invested capital,
33 which increased the amount of taxes, and he made additional assessments against these corporations which they paid. That was prior to March 7, 1921. In other words, the commissioner did not finally determine the taxes upon the amount of the income as returned. He changed it, adjusted it, and corrected it.

Then in March, 1921, the commissioner—or prior to that he made a further examination and then he issued another letter in which he further still increased the income. He made a slight increase in invested capital, but increased the income to the extent of over five million dollars, and that increase was based on a change in the basis on which these corporations had valued their normal stock of tin plate.

The commissioner ruled and determined that the basis on which they had valued their tin plate at a constant figure was not correct, or permissible under his regulations that the income should not be determined on the basis on which they kept their accounts and made their returns, but that it should be determined on the accrual basis as defined by his regulations.

Your honor will perhaps recollect that during the early part of these income tax laws the regulations of the department about the determination of income and so forth were not definitely crystallized, the thing developed gradually. The revenue act of 1917 was the first act which imposed the excess profit tax. Prior to that time there had been only a small income tax at a small rate, one or two per cent, and the matter of checking up the income and verifying it and establishing the rules for computing it had not become particularly important, and it was not until after the excess profit tax arose that a great many additional questions arose, and the commissioner worked those questions out gradually, but it was not until along in 1919,

after the 1918 revenue act had been passed, that he had a comprehensive system of rules and regulations that covered all the
34 points that were apt to arise in the matter of determining the income of corporations and valuing their inventories upon the accrual basis of keeping accounts.

That is reflected a little in the history of this case, because on the first examination of the returns of this corporation the commissioner made no objection to the method which the company had used in valuing its inventory. And it was only after a further examination that he objected to the method on which they had valued their inventories, and then the commissioner determined that the income of these corporations for the purposes of the 1917 tax should be determined upon the accrual basis in accordance with these regulations which he in the meantime had been establishing, issuing, and promulgating, and that the inventories must be valued in accordance with his regulations, and his method was—well, your honor, we need not go into the technical details here. I am just giving the principle to your honor.

Now, all the taxes which these corporations paid prior to March 7, 1921, were paid to William H. Edwards, who was the collector of internal revenue in New York, and he was not in office as collector when these suits were commenced. That is the reason we are here in the District Court suing the United States instead of suing the collector.

The other taxes which were assessed after March 7, 1921, and which we, of course, had to pay, those taxes were paid to Frank K. Bowers, who is now the collector of internal revenue.

The COURT. In New York?

Mr. SUMNER. In New York, and he is still in office, so our suit to recover those taxes was brought against Bowers in the District Court in New York, and those taxes are not involved in these suits. Under the statutory procedure, it is impossible to consolidate them unless they are all brought in the Court of Claims, but when we bring
35 suit in the District Court we have to sue where our residence is—under the Tucker Act—and when we sue the collector in the District Court we have to sue where his residence is practically. So the only taxes your honor will be concerned with here are those which these corporations paid prior to March 7, 1921, to William H. Edwards, collector.

Now, these corporations take the position in a nutshell that under the revenue act of 1917, the cash basis for determining income was the primary and fundamental basis prescribed by Congress. And there was no provision in that statute authorizing the determination of income upon any basis other than cash basis, except a section which is called section 13, subdivision D. That section provided in substance that a corporation which kept its accounts on a basis other than a cash basis might make its return on the basis on which it

kept its account, if that basis clearly reflected its income, in which case the tax should be computed on the income as returned. That is all it says. That is to say, provided that if the corporation made its return on the basis on which it kept its accounts and if that basis clearly reflected income then the tax should be computed on the income as returned.

The commissioner has ruled and determined in these cases that the basis on which these corporations kept their accounts and made their return did not clearly reflect their income, and hence he ruled that the tax should not be computed upon their incomes as returned. And it is our contention that under those circumstances this section 13, subdivision D, has no application and the income must be determined upon the cash basis under section 12a of the act, which prescribes the cash basis as the primary basis for determining income. And we have alleged and expect to prove that if our incomes are determined upon the cash basis, they would be very much less than the amounts which we returned. If your honor follows what I mean.

36 The COURT. Yes, I do. In other words, on the accrual basis you would include an income of bad accounts.

Mr. SUMNER. We might to some extent; yes. But really you never can tell what the difference is going to be in any particular year until you figure it. There cannot be any presumption that it will be larger on one basis than the other. In one year it might be larger on the accrual basis and smaller on a cash basis and vice versa.

The COURT. The commissioner having ruled that you should make the return upon the cash basis you say that is the end of it.

Mr. SUMNER. That is practically it; yes, sir.

The COURT. In other words, having decided the question he is estopped from reversing his decision. I am only getting your adversary's point of view clearly in my own mind, Mr. Hendler, and then I will see if it holds out.

Mr. SUMNER. It is not quite as brief as that. It is our position that the statute prescribes the cash basis in the first instance, and simply has this permissive section, section 13, subdivision d, which says in certain cases the taxes shall be computed on the income as returned. The commissioner has ruled in substance that this is not one of those cases. He ruled that the basis on which we kept our accounts and made our return did not reflect our income and that the taxes should not be computed on the income as returned, and hence it follows that section 13d is not applicable at all, and the only one applicable is the one determined by Congress, the one for determining income on the cash basis. And, therefore, we contend that our tax be redetermined on the cash basis and that we recover back the excessive amounts we have paid on the basis of our books and pursuant to the other assessments made by the commissioner.

The commissioner took the view that section 13d by implication gives him authority in the case where the return does not clearly reflect income to redetermine income on the accrual basis in
37 accordance with his regulations for valuing inventories and so forth. Whereas, there is not a word in the statute which confers upon him any such authority.

It seems to us that he has assumed to himself authority to redetermine income the way he thinks that it ought to be determined for convenience in connection with the administration of this law and in doing so he has gone beyond the authority Congress undertook to confer on him in the revenue act of 1917. And that point is definitely illustrated in this way, because when Congress passed the revenue act of 1918, the following year, it very definitely provided that the income should be determined in the first instance upon the basis upon which the accounts were kept—it did not prescribe the cash basis—if that clearly reflected income and if it did not then they should be determined upon such basis as the commissioner might prescribe. So there was a very definite grant of authority to the commissioner in the 1918 law to prescribe a basis for determining income and under the well settled principle the fact that Congress in the subsequent act made that definite grant of authority by language which is entirely different from any in the former act, our income should be determined upon the cash basis.

Another thing Congress did in the 1918 law was to give the commissioner express authority to determine the basis upon which inventory should be valued. There was not a word in the 1917 law about inventory, the reason being that where you are working on cash basis you do not use inventory. That is the difference between what is actually received and paid out in the year, it is all cash in and out, and there was not a word in that law about inventory. But in the 1918 law they gave him express authority for establishing a basis for valuing inventories.

The whole substance of the 1918 act is different from that of
38 1917 and earlier acts in that they give to the commissioner wider power to determine income under general regulations prescribed by him, whereas the theory of the former act was to prescribe in the acts themselves the basis for determining income as the cash basis, and it is only in this permissive provision, I refer to section 13d, that Congress recognized in the 1917 act that under any circumstances income could be determined upon a basis other than the cash basis.

Now, of course, your honor is familiar with the recent state of law with reference to actions to recover back taxes, and I think it is fair to say that under the revenue acts since 1923 it has been a very definite policy of the law to permit taxpayers to correct mistakes and recover back any and all overpayments they may have made, whether paid under protest or duress, and the revenue act says that whenever an overpayment of taxes has been made the amount shall be repaid to the taxpayer immediately, unless it is credited to some other tax

Of course, it is still necessary to file claims for refund with the collector first. And we filed them in this case and they were based on the same theory that inasmuch as the commissioner had definitely ruled that the tax should not be based on the basis on which we kept our accounts and made our returns that the only alternative was the cash basis prescribed in the statute; and hence we are entitled to have the income returned on the cash basis and recover the amounts we have overpaid.

That gives the theory of this thing in a nutshell and practically all of the allegations in the petitions, nearly all of them have been admitted by the answers. There are one or two matters where there are some figures to be proved, which I think there is no dispute about beyond that our burden will be to prove the income of these corporations—actual receipts, actual disbursements——

The COURT. Have you had statements of these incomes taken off the books and submitted to the Government?

Mr. SUMNER. Right after the answers were filed, the United States attorney wrote to Judge Treacy, who was attorney of record, in which he said this: "I should suppose it would be possible to stipulate the facts and submit the matter on proof. Have you any suggestions along this line?" And Judge Treacy replied to that: "I fully agree with your idea of stipulating the facts and suggest that you arrange to have the books and accounts of the plaintiff examined in order to verify the allegations of fact which may not be within your knowledge."

Of course, the petitions themselves state the amount of the net income on the cash basis. But it does not show the details of the computation. That letter was written on May 8, 1926, and later, on July 21, Judge Treacy sent the United States attorney a proposed stipulation covering all the facts that were not admitted by the answer, and that stipulation was never made. It seems it was sent to Washington, I believe, and no definite ruling on that developed until quite recently. And in the meantime, we made our preparation to prove these facts of income on the cash basis. But what this does show is that we have been perfectly ready and willing, since May of last year, to allow the Government to examine our books and records in order to check up and verify these figures, but they have not availed themselves of the opportunity.

The COURT. Now, what about the defense to the action?

Mr. HENDLER. If your honor please, in the statement of my friend it would seem as though the question involved here was a very complicated one. But I imagine that when it comes to sift down your honor will find it rather a simple one.

It is true that under the earlier acts—that is, the act of 1909, which was the corporation excise act, the provisions of which were that excise tax should be measured by the net income of the corporation—and it has been held that that provision in the excise tax act was in effect, with regard to net income, in fact the same as provisions with regard to net income in the later income pro-

visions of the tax act, but it is none the less true that it was early discovered that it would be impossible to administer the earlier income tax act and the corporation excise tax act, unless some provisions were made for what is the universal practice, certainly of the larger corporations if not of all corporations, of keeping their taxes on the accrual basis. Permitting that system of accounting to enter into the returns and the payment of the income tax developed by that system of accounting. There is no question at all—while I am on that point—well recognizing that the department issued a regulation permitting corporations to make and file their returns on the accrual basis just as their books were kept, provided the returns so made should clearly reflect their annual income, and practically all corporations, among them this corporation, took advantage of that provision of the regulations.

That regulation has been sustained by the Supreme Court in reversing the Court of Claims in two cases. Now, this corporation consistently—and there is no question about that—up until it came to make its return for the year 1917 kept its books and made its return on the accrual basis. It made its return for 1917, and that is the contention of the Government, it made its return for 1917 on the accrual basis, and it is our contention that having begun and continued through the years making its returns on the accrual basis, which was permitted in paying its tax, that it can not shift its position to any other than the accrual basis.

Now, there are only two basic methods for accounting and they are the cash receipts and disbursements or the accrual basis. Here is what happened for the year 1917, it had made all its inventories on the basis of cost, both its openings and its closing inventories preceding 1917, so that its closing inventory on the 31st of
41 December, 1916, was on the basis of cost. It paid its taxes on that accrual basis, a part of which was represented by its closing inventory for the year 1916 on the basis of cost for its materials.

Now, it went along and no change was made. Of course, our contention is that no change ever was made in the accounting system of the claimants here, nor did the commissioner by his ruling change the method of accounting or returning of the claimant, but it developed late in January, the end of January, 1917, the price of the claimants' raw materials suddenly jumped in the market. The price theretofore had been practically, if not absolutely, staple at $3.60 a box. At the end of January that price had jumped to $7 a box. As I pointed out to your honor, they made their closing inventory and paid their taxes on the basis of the cost of their materials at $3.60 a box; but they held a meeting of their directors on the 31st of January and they determined that they would establish a stabilizing system by which they would set up an arbitrary number of boxes of tin plate which they refer to as their normal supply, and opened what they called an inventory constant account to which was credited the difference between $3.60 a box and $7 a box.

Now, when they came to make up their inventory, their closing inventory, at the end of the year 1917, everything else in the return was made and all of their accounting was done on the accrual basis, but when they came to make up their inventory at the end of 1917, their closing inventory, they discarded entirely this difference. I think the number of cans which they called their normal supply—now that is an arbitrary figure which they set up and, of course, arbitrary figures can play no part in a correct inventory—they deducted from their closing inventory this credit which had been made to their so-called constant inventory account. The contention of the
42 Government is that when the Commissioner of Internal Revenue said "No, you can not establish any such arbitrary figures in making your inventory," he did not determine that they should not make their return on the accrual basis. They had done it theretofore up until 1917 and their inventories were made on the basis of cost. That is admitted prior to 1917, and all that the commissioner did was to insist that the system which they had theretofore followed consistently must be followed for the year 1917.

Now, therefore, the position of the Government is that the commissioner in his ruling requiring simply the correction of a manifestly erroneously wrong inventory does not change the basic method of accounting, and manifestly not. Suppose, if your honor please, upon investigation it should be found that a taxpayer in making its closing inventory for the taxable year had omitted to include in its inventory certain property which under the law, as the commissioner interprets it, should be included in that inventory. If the commissioner holds that the taxpayer, after an investigation of the books of account of the taxpayer, should have included that in its return or in its inventory, does that change the basic method of accounting? Does the commissioner if he discovers merely—and it is in nowise different in principle—if he discovers that the taxpayer has made a mistake of one million dollars in adding up the totals in its inventory and he insists on that being corrected, does that change the basic method of accounting? The courts have sustained and, of course, it is reason and common sense the ruling of the department, that the inventories shall be taken at cost or market, whichever is lower, and, of course, that is not any hardship to the taxpayer. In one year it might lead to the payment of a trifle more than otherwise if one figure or the other is taken, and the next time when the tax is paid upon an inventory at the figures which closed the preceding year it equalizes.
43 But I want to direct your honor's attention particularly to this fact, that this complainant, this claimant here, for every year preceding 1917 kept its books, made its returns, and paid its taxes on the accrual basis. Now what does that mean? When it came to make its return for 1916, it, of course, included in that account whether it was paid in 1916 or paid late in 1917 every dollar of indebtedness which accrued in 1916, the bills payable—I have not the slightest doubt, for all, and certainly if not for all for most of the

tin plate as to which it changed its inventory figures. Now, manifestly, if the court please, in rendering an inventory, the closing inventory, for one year is the opening inventory for the next year. The figures must be the same. And then when we come to the year again a taxpayer arbitrarily sets up some figure simply by opening an account called an inventory constant account. Now, as to accounting by the corporation with its stockholders, or with its bondholders that is an entirely different matter. We are dealing with a very practical matter of taxation.

Now, 13d, about which my friend talked, but he paraphrases and generalizes with regard to it—I do not mean that criticism, of course, it would not become me. But subdivision D of section 13 of the revenue act of 1917—now your honor will probably recall that the act generally referred to is the revenue act of 1917, was passed in October, 1917, and its main purpose—we actually entered the war the preceding April—its main purpose was to increase the revenue on account of the war. There was some amendment to the provision of the 1916 statute, but the main purpose of the statute was to increase rates, and among those amendments was this subdivision d of section 13, and it was seeking to carry out the commonsense idea that corporations, as I said in the beginning, which universally kept their books on the accrual basis, might be permitted to make their returns on that basis in accordance with the statute.

Now this is the way subdivision d reads: "A corpora-
44 tion, joint stock company or association, or insurance company, keeping accounts upon any basis other than of that of actual receipts and disbursements"—now, there is not any question that this corporation kept its books on the accrual basis. My friends will raise no questions about that. "Unless such other basis does not clearly reflect its income, may"—now that is the important part about this subdivision—"subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned."

Now, later on the commissioner in Treasury Decision 2609 in the regulations that were made, and they had to be hurried because of the passage of the October act, in the regulations that were made it was announced that later regulations would follow showing what would be required in making inventories, and by Treasury Decision 2609 that regulation went forward.

Mr. SUMNER. What was the date of that?

Mr. HENDLER. December 19, 1917. My friend, when we get to the argument, will make some point of the lateness of the year in which that regulation went out, but it was reasonable. It simply did what the earlier ruling of the department permitted the taxpayers to do. The commissioner has not changed the method of accounting. He has permitted the taxpayer to make his return on that basis.

The COURT. May I intrude a minute? It is running through my mind and may not have any bearing on this case at all, but my recollection is that manufacturers in 1917 were very much perturbed by the advance in the cost of raw materials. The fact that they did advance very rapidly in cost, necessitating additional capital to carry on the business; that is, the inventory of today having been purchased we will say for one hundred thousand dollars could
45 not be replaced except by the expenditure of two hundred or three hundred thousand dollars. That required a certain exception. Now, I wonder if that had anything to do with these rulings?

Mr. HENDLER. None in the world.

The COURT. Was that circumstance one of the reasons why the American Can Company was creating this inventory constant? Was that the reason the directors were setting it up on their books in some way or other because when they came to replace their inventory they would require additional capital to carry on their business?

Mr. SUMNER. They had to buy in advance. I think your honor's thought very nearly fits the point. They had to buy in at the high price and they figured that it would not be sensible from a business point of view to figure anything different than what it would cost them constantly to get the material.

The COURT. A man is carrying on business and he has one hundred thousand dollars invested, fifty thousand dollars in raw material which he needs in his business. The price immediately jumps two or three times for the replacement of those raw materials. Now, he can not stay in business unless he can get additional capital in his business, because he must have fifty thousand dollars' worth of goods to carry on and the price of those goods has gone to one hundred and fifty thousand dollars, he has to get one hundred thousand dollars additional somehow or other to carry on his business the next year.

Mr. SUMNER. He has to pay it out as he goes along.

The COURT. Exactly.

Mr. SUMNER. In order to keep himself in business.

The COURT. It is the same proposition as if a lawyer has one hundred thousand dollars in bank, and says, "This is the money I carry my business on with." Everything that he buys goes up three times, and he has to have an additional two hundred thousand or has to close his shop.

46 Mr. HENDLER. Yes; that may all be true, and for that reason I say that it is not pertinent to the question here involved.

The COURT. That is what I wondered.

Mr. HENDLER. That lawyer if he maintains his one hundred thousand dollars or fifty thousand dollars or twenty-five thousand dollars in bank from his earnings during the year, notwithstanding he keeps it in bank, it is just as much income to him as any other profit or gain derived from his business. The fact that a corpora-

tion out of its earnings during the year carries to its surplus account any portion of the earnings it received during the year is not relieved from paying an income tax on that portion which it carries to surplus. That is as much income as the earnings they paid out to the stockholders.

The COURT. Possibly that circumstance that raw materials were advancing on the market was the reason that when the 1917 act was drafted it provided for the payment of a tax upon the cash basis—the language shifted to cash basis.

Mr. HENDLER. No; your honor.

The COURT. That this provision that 13d might apply where the accrual basis actually reflected the income received. I was wondering whether Congress did not have in mind the practical circumstance that business men in the country were terrifically embarrassed in their accounting system by reason of the great advance in the cost of their materials.

Mr. HENDLER. No, your honor, the 13d was incorporated in the 1917 statute to take care of what was a perfectly well known fact, that the accounting system with practically every corporation is and was and always has been on the accrual system. This corporation could not do business for five years consecutively unless it did its accounting on the accrual basis. Now, what happened? It is only a guess, of course, I am not criticizing the conservatism of a corpora-
47 tion in casting an anchor to windward, if I may so term it. Every person almost, except the extreme pacifist, recognized in January, 1917, that this country inevitably was going to war with Germany. There appeared in January and during February and March no escape for the United States except to go to war.

The COURT. As I recall, President Wilson was elected on the slogan "He kept us out of war."

Mr. HENDLER. But almost immediately there was a development of a return by Germany to the sinking, without warning, of vessels all over the world. But as I was about to say, if I might be permitted to guess as to another reason beside that conservatism, which I say I do not criticise, it was this. When the prices did jump they were then confronted by a condition and not a theory, and when the prices did jump they did not want to go before their stockholders and their bondholders later—of course, the situation as it affected them then, and I imagine they were no different from the other large corporations that immediately began to develop large earnings or had had large earnings during the war period, but they realized there was coming a time when after driving ahead and continuing to drive ahead, the prices of their raw material and, of course the prices of their finished product, were going to slump and their earnings would be materially curtailed on account of that—the material for their finished product decreased—and buying their raw material at a high figure they would suffer incidentally a loss in their inventories that would necessarily affect their dividends to their stockholders.

Now then, you cannot take care in taxation matters of the losses that might be sustained in a subsequent year. Each year must take care of itself in the losses and gains. If this corporation having bought and paid for in 1916—because that is really what happened—for the tin that it had on hand at the beginning of 1917, if it disposes of that tin in the shape of a finished product, the revenue
48 act says that gains and profits from all sources must be returned as income. If a taxpayer disposes of assets at a price beyond that which he paid for the assets, the difference between the two is income to him, and it would be utterly impossible, as your honor can see, to shift the position after having accrued their income in the preceding year, to ever place them in the same situation at the beginning of 1917, except by continuing the method of accrual.

If there is any person to be criticised, if your honor please, about any delay in reply to this correspondence which was before your honor, I am the guilty party.

The COURT. That is no criticism. My inquiry was simply directed to this point, that it seemed to me that if they could offer in evidence their condensed balance sheets and the Government had had an opportunity to have accountants look over their books that a great deal of time would be saved.

Of course, if their balance sheets are incorrectly made and improperly made up that is a matter that can be easily determined by an accountant, and it is far cheaper for the Government to send an accountant over to go over their books than it is to spend so much time here in going over those books.

Mr. HENDLER. Yes; but the availability of the proper men to go to the headquarters of these corporations—

The COURT. But look at those books. They are not a bit available for a court either. If the Government is in dispute as to their facts it seems to me that they could quite readily go through the thing and see. I apprehend that the American Can Company and its accountants keep their books correctly, because they are too large a concern to do otherwise.

Mr. HENDLER. I assume that is so.

The COURT. I was rather prepared to let them offer their condensed balance sheets and have them marked in evidence, and
49 then you and your accountants can examine their books and see what your cross-examination might be, and I will take a recess while you are doing that.

Mr. HENDLER. It would take months to go through those books; that is just what I was about to say, or weeks or days, anyhow.

The COURT. Of course, they make returns to the New York Stock Exhange and they make returns to their stockholders.

Mr. HENDLER. Of course. Now, as to the balance sheet, there is practically no question here as to the balance sheet. I mean there is no materially essential question as to that except as to their inventory. This whole case revolves itself around that question of in-

ventory. That is the real nub of this case. There is no question their balance sheet will demonstrate beyond peradventure, their condensed balance sheet which accompanied their return for the year 1917, is on the accrual basis, just the same as their 1916 balance sheet was. Is not that so?

Mr. SUMNER. The return was made on the accrual basis, of course, the basis on which we kept our accounts with this normal stock method of valuing inventory.

Mr. HENDLER. Of course, the method of making that inventory does not develop in that condensed balance sheet. It is only by the field examination that it was developed that that was their method of making up their inventory. I say again there is where I sought to interrupt counsel, replying to your honor's question that the Commissioner of Internal Revenue never did require this taxpayer either to keep its books or to make its return on the basis of cash receipts and expenditure. I do not know whether I have made myself clear.

The COURT. I think you have made yourself beautifully clear.

Mr. SUMNER. I think perhaps it will pay to spend plenty of time at this stage of the case in order to get our different points of view clearly before your honor.

50 With reference to the time of this matter, I think your honor will recall that we declared war on Germany April 7, 1917, and that really there was nobody in this country who knew whether we were going to declare war or not until a few days before that declaration was made. The country was wondering what President Wilson's position was to be and how long he was going to keep the country out of war, admiring his patience and endurance with the thing going on, and as I recollect it was not until he wrote his war message to Congress in which he finally recommended the declaration that the public saw that we were in war, and that was a few days before the declaration.

It is true that the prices of tin plate went up decidedly early in January, 1917. That was not because of the expectation this country was going in the war. It was because of the demand for munitions from foreign countries. This country had been in the business of making munitions for some of the foreign governments, and the prices began to go up in 1916 as a result of the extraordinary demand for the products of this country from foreign governments. This company in 1917 sat down and said: "Here we are buying seven or eight million boxes of tin plate a year to keep our business going at 3.60 a box. That is pretty close to twenty-four million dollars." Now the price goes up to $7. We have to pay fifty million dollars this year for tin plate. We can not afford to compute our income for this year on the basis of what we paid for tin plate last year. It is not fair to ourselves or stockholders. It does not reflect what our plants are doing. We have to pay our way as we go," and it was for that reason that they put into effect early in the year, before the

end of January, this normal stock method of valuing tin plate, and it was a situation that had not developed ever before in this country. They were never confronted with a similar situation, and you can see that it was not inconsistent with anything they had done
51 before. We cross our bridges as we get to them. When we come to war time and extraordinary abnormal conditions, we have to use appropriate methods in our accounting to meet it, and that is what these men did. And I do not think anyone would question that it was sound and proper from a business point of view, for them to carry their stocks at a constant figure during the year and not treat the abnormal increase in the inventory value of their tin plate stock as actual income, as everyone knew that the increase was temporary. It would go down later.

There is a very singular similarity between the cash basis and the normal stock basis. As your honor already indicated, it is quite obvious that when you are computing your income on the cash basis you take into your gross income what you collect this year and you charge against that what you pay out this year, so if this company had kept its books on the cash basis it would have had to charge against its income for 1917 the amount it was paying in 1917 for tin plate it was buying in 1917, and that is exactly the basis which section 12a of this revenue act prescribes as the primary basis for determining income. When you keep books on the accrual basis, but with normal stock method for valuing inventories, you arrive at somewhat the same result as a matter of principle.

The COURT. I understand that.

Mr. SUMNER. So it would be our point if we got into an argument whether it was proper or not that what we did with the normal stock basis was more or less justified by the provisions of the statute.

I do not want to go into an extended argument here as to whether that method we used was correct or not, as I do not think it is involved in this case. I want your honor to appreciate that we put it in effect before the war and before there was any high rate of taxation, and it was a reasonable business method in the interest
52 of the stockholders of this corporation and not a tax-dodging scheme.

The COURT. Let me see if I have the idea. You adopted this arbitrary inventory constant as a short cut for the determination of what your directors actually believed their income to be.

Mr. SUMNER. Yes, we do not say it was arbitrary, but we put these entries on our books.

The COURT. It was your short-cut method. When that was submitted to the commissioner, he said, "No; you cannot do it that way," and you say, "Since our method of keeping books on the accrual basis does not reflect our income, we will have to revert to the cash basis, otherwise we will be ruined."

Mr. SUMNER. Your honor has absolutely got the mainstay of this case.

The COURT. It is somewhat analogous to the conservative banker. Bonds advance in the market. The conservative banker does not charge them up on his books as income. He holds them somewhat below the market so that when they drop down again he may have an avenue of safety, and may not have to reflect a loss in his statement of a considerable amount of money. Is that the idea?

Mr. SUMNER. You have got the point exactly, and your honor will see in that connection that we are not here to argue whether the regulations the commissioner issued about how inventories should be taken on an accrual basis were right or whether our basis we used is right, but we are here to say that as a matter of law the commissioner having said our method was wrong and he will not accept it, the only alternative is the cash basis. And I think that our interpretation is fully sustained by these contemporaneous rulings to which my opponent has referred which were approved by the Supreme Court, because that was in January, 1917.

If your honor will look at page 19 of my brief, that is
53 an extract from the opinion of the Supreme Court, and it refers to this ruling of the commissioner which was under the 1916 law, but it had this same subdivision 13d in it. He said that the accrual basis was permissible provided that the taxpayer accrued his receipts as well as his disbursements, "and provided that if returns upon this basis of accruals or reserves did not reflect true net income, the taxpayer would not be permitted to make its return on any other basis than that of actual receipts and disbursements." Practically recognizing at that time that the only alternative, if the basis the taxpayer used was not proper, the only alternative was to go to the cash basis. And in the next sentence he says, "We think that the statute was correctly interpreted by the commissioner and that this decision referred to was consistent with its purpose and intent."

Perhaps your honor is familiar with this revenue act and these sections we have been talking about.

The COURT. Of course I am not familiar really with anything. That is always a proper assumption for a lawyer to make.

Mr. SUMNER. I did not want to simply waste time in talking about things your honor knows more about than I do.

The COURT. I have had a few of these income tax cases.

Mr. SUMNER. If you will look at page 8 of my brief and follow that page through for a minute, you will get this language with the exact words of the statute. Perhaps you should start at the bottom of page 7. Under the revenue act of 1917 there were really two kinds of taxes, one income tax and the other the excess-profit tax. Income tax was straight percentage on income, 6 per cent. And the excess-profit tax depended both on invested capital and income, the rates of the tax depending on the amount of the invested capital.

54 Now, the statute provided that the tax was imposed on the total net income received by every corporation, and then in title 2 of the revenue act of 1917, section 206 provided that "for the

purposes of this title the net income of a corporation shall be ascertained and returned * * * for the taxable year upon the same basis and in the same manner as provided in title 1 of the revenue act of 1917." Section 12a of title 1 says that in the case of a corporation organized in the United States such net income shall be ascertained by deducting from the gross amount of the income received within the year certain expenses, taxes, and interest paid within the year and certain losses sustained and charged off within the year."

Now, the whole description of these expenses, and so forth, are more or less accurately described.

Then the next section, 13a, says "that the tax shall be computed upon the net income, as thus ascertained, received within each preceding calendar year." Now that is the main body of the statute.

The COURT. Yes.

Mr. SUMNER. And this section 13d of title 1, which is set out in my brief verbatim, I do not want to dodge a single word——

The COURT. I understand page 9 is your interpretation of it.

Mr. SUMNER. Yes. That subdivision created an exception to the general rule that was laid down in the body of the act. There was no exception mentioned in the body. It was an universal cash basis for everybody, and this is added on, and it is perfectly obvious under well-settled rules that it can only operate in so far as it is directly inconsistent with the general rules. No power of the commissioner can exist by mere implication. The commissioner has no powers under a revenue act except such as the act clearly confers upon him, and it is not open to the commissioner by any kind of regulations to add something to the statute which is not there. The pur-
55 pose and intention of regulations is to carry out the provisions of the act as laid down by Congress. The regulations do not help a particle to find out what his powers were in this case, as Congress said what his powers were, and he cannot create powers himself by any kind of regulations.

Now, regarding the proof of the figures of the income on the cash basis, we have a brief summarized statement showing the gross amount of the income received and the amount of these deductions.

The COURT. What I ordinarily do in matters of that kind, and I think Mr. Wigmore supports me, is to let the accountant go on the witness stand and testify that he has made up that statement and it is true, and I let them cross-examine if they want to and then I mark the thing in evidence.

Mr. SUMNER. I think that is the only way to do it, because in addition to these books we have a truck load of documents down at the door.

The COURT. I think Mr. Wigmore supports my ruling, and I have been proceeding that way for some time. Until I am told I can not do it, I shall proceed to do it.

Mr. SUMNER. The biggest point about getting up that kind of a statement is to make the proper allocation between capital and in-

come items. We can prove the total amount of cash received and total amount paid out, but a lot of that is capital received and capital paid out, and our problem is to allocate and separate the two, which we have done with the greatest care possible. And the United States Government has sent revenue agents to check up our books from 1909 to 1923, inclusive, and they have been over everything they wanted to see and they have ironed out every possible question as to what is an income item and a capital item. And they have had an opportunity for the last five years, if they wanted to, to send men up from Washington to check up this thing, as it was involved before the Bureau of Internal Revenue when we were
56 down there on our claim in abatement, and it is all set out in the claim for refund which we filed. Shall I proceed with the witness, your honor?

The COURT. Yes.

CHARLES E. GREEN, called and sworn as a witness in behalf of the plaintiffs, testified as follows:

(Counsel confer.)

The COURT. What is the problem now?

Mr. SUMNER. Mr. Hendler has the original income and excess-profit tax returns which he brought up from Washington, and I was just suggesting that it was not necessary to put them in evidence at all. All I wanted to do was establish certain figures which were contained in the return, which we can probably do by stipulation.

The COURT. Put them in subject to correction, if incorrect.

Mr. HENDLER. In explanation, if your honor please, I did not discover until I landed in the city yesterday that the photostat copies of a large mass of these papers, which had been forwarded from our office to the United States attorney's office here, had never been received. To my utter astonishment I found that.

The COURT. The only suggestion I was making was that anything in the way of income-tax returns that counsel desires to put in that he put it in now, subject to correction if incorrect.

Direct examination by Mr. SUMNER:

Q. Mr. Green, will you give your full name, please?
A. Charles E. Green.
Q. What is your occupation?
A. Comptroller of the American Can Company.
Q. And also of its subsidiary companies?
A. I am auditor of the subsidiary companies.
Q. How long have you been comptroller of the American Can Company?
57 A. Since October 1, 1926.
Q. Prior to that time what was your occupation?
A. Auditor of the American Can Company.
Q. How long had you been auditor of the American Can Company?
A. Since February, 1907.

Q. Have you, generally speaking, also been auditor of the subsidiary companies since February, 1907?

A. Yes.

Q. Did the American Can Company in 1917 own substantially all of the capital stock of the following-named corporations: The Missouri Can Company, Detroit Can Company, American Can Company of Massachusetts, American Can Company of Utah, The Sanitary Can Company, The Charles W. Shonk Company, The Union Can Company, The Davenport Can Company, The Newton Manufacturing Company, The Wade Machine Company, the Raleigh Manufacturing Company, and the Newbern Box Company?

A. It did.

Q. Those were all corporations organized in the United States?

A. They were.

Q. And the American Can Company did not own substantially all the capital stock of any other corporations organized in the United States?

A. They did not.

Q. Did all of these corporations which have been mentioned keep their accounts during 1917 upon the basis of accruing their receipts and disbursements valuing normal stock of tin plate carried in their inventory at a constant figure, regardless of changes in the cost or market value of tin plate, and valuing the other materials carried in their inventories at cost or market value, whichever was lower?

Mr. HENDLER. I do not think we ought to go along that way. It is leading the witness. It is a picture of what they actually did. If we have made ourselves plain you understand what that means, but if that comes in cold type before some person who has heard no such discussion they can not appreciate what that means.

The COURT. I suppose Mr. Sumner might say, "How were the accounts kept prior to 1917," and then this gentleman would say that they were kept on the accrual basis and the inventory was marked out on whichever was lower, market or cost.

Mr. SUMNER. I admit that the question was leading, but I did not suppose there was any dispute. I will withdraw it.

Mr. HENDLER. I am not objecting simply because it was leading, but to let us have a record that anybody can understand.

Mr. SUMNER. Well, it seems to me, your honor, that if there is no objection on the ground that it is leading, that the witness is qualified to answer, he being the chief accountant and an officer of this corporation and familiar with its accounts for more than twenty years.

The COURT. I think that is well taken.

A. They did.

Q. Was tin plate one of the most important materials which these corporations carried in their inventories and used in their business?

A. It was.

Q. What was the business of these corporations?

A. The manufacture of tin cans and sheet metal and fibre containers.

Q. And to some extent did they manufacture munitions at this period?

A. And munitions.

Q. Now, these corporations all made and filed Federal income and excess-profit tax returns for the year 1917?

59 A. They did.

Q. And they were filed, weren't they, with William H. Edwards as collector of internal revenue in New York City?

A. They were.

Q. Were these income and excess-profits tax returns made upon the basis upon which the accounts of these corporations were kept?

A. They were.

Q. And did the American Can Company on or about June 14, 1918, pay to Edwards as collector of internal revenue, and did he collect from the American Can Company the amount of the taxes, income, and excess-profit taxes, payable in accordance with the invested capital and income stated in the returns?

A. The company did pay and the collector accepted such taxes.

Q. Is this check of the American Can Company dated June 14, 1918, the check by which such taxes were paid?

A. It is.

Q. And you know the signatures of the officers of the American Can Company appearing on that check?

A. I do.

Q. Are they genuine signatures?

A. They are.

Mr. SUMNER. I offer the check in evidence.

Mr. HENDLER. If you will show me all the checks maybe we can agree.

Mr. SUMNER. All right.

Mr. HENDLER. We admit the payment of that $3,266,499.86 shown by that return.

Mr. SUMNER. Are you going to dispense with the check?

Mr. HENDLER. Oh, yes.

Mr. SUMNER. Then I had better complete it (continuing). To Edwards, as collector of internal revenue on or about June 14,

60 1918, as and for income and excess-profit taxes for 1917, payable by the American Can Company in accordance with the amount stated in its income and excess-profit tax return.

Mr. HENDLER. I guess that is all right.

The COURT. Let me see the check [check handed to court].

Mr. SUMNER. Sometimes it is simpler to put the checks in evidence.

The COURT. Have you got photostats of this check here?

Mr. SUMNER. No; but we can easily get them. We are perfectly willing to have the check marked in evidence and then we can get a substitute photostat copy.

The COURT. Why don't you do that? Now, Mr. Sumner, let me make a suggestion. You have several of these checks which you really want to mark in evidence. Why don't you just tell counsel for the Government which ones you want and let him check them, it being stipulated that the plaintiffs herein named substitute for these checks offered in evidence, one photostat copy for the court's record, and one photostat copy for the Government?

Mr. SUMNER. I offer in evidence the checks showing the payment of the income tax and the excess-profit tax for 1917 of the American Can Company, the Detroit Can Company, and the Missouri Can Company, which are marked in evidence P–1, P–2, and P–3. It is stipulated that photostat copies of these checks may be substituted for the original vouchers of the companies.

(Received and marked "Exhibits P–1, P–2, and P–3.")

61 Mr. SUMNER. I suppose it can be stipulated also that the amounts of these checks correspond with the amounts of the tax as shown on the returns computed on the amounts of income and invested capital shown on the return.

The COURT. Yes.

Mr. SUMNER. There is no dispute about that, is there?

Mr. HENDLER. No.

Mr. SUMNER. It is stipulated that the amount of the net income of the American Can Company for 1917 as returned was $16,927,404.35, including $60,010.50 as dividends from other domestic corporations, and the amount of the consolidated net income of the American Can Company and all its American subsidiary companies as returned was $17,994,400.46, including $60,010.50 as dividends from domestic corporations. And that the amount of the consolidated invested capital of the American Can Company and its American subsidiary companies for 1917 as returned was $97,019,377.66. That is stipulated, is it not?

Mr. HENDLER. Yes.

Mr. SUMNER. This plaintiff offers as plaintiff's Exhibit P–4 the income and excess-profit tax return of the American Can Company for 1917, as P–5 the income and excess-profit tax return of the Detroit Can Company for 1917, and as P–6 the income and excess profit tax return of the Missouri Can Company for 1917. It is stipulated that the Government will substitute for these original tax returns certified photostat copies hereof.

Mr. HENDLER. Yes.

(Received and marked "Exhibits P–4, P–5, and P–6.")

62 Q. Mr. Green, have you made a computation of the net income of the American Can Company and its American subsidiary companies for the year of 1917 on the cash basis?

A. I have.

Q. Does that paper that you hold in your hand show the result of that computation?

A. It does.

Q. Is that computation based on the books and records of the American Can Company and its subsidiary companies?

A. It is.

Q. Were they regularly kept in the ordinary course of business pursuant to a general system of accounting?

A. Yes, sir.

Q. Is this computation correct to the best of your knowledge, information, and belief?

A. It is.

Q. Does it show correctly the amounts of the gross income of the American Can Company and each of its American subsidiary companies for 1917 as received in the year 1917?

A. It does.

Q. Does it also show correctly the amount of the ordinary and necessary expenses paid in 1917 by each of these corporations in the maintenance and operation of its business and properties?

A. It does.

Q. Does it also show correctly the amount of loss actually sustained and charged off in 1917, and not compensated by insurance or otherwise?

A. It does.

Q. That is true of the case of each corporation?

A. Yes.

Q. Does it also show correctly the amount of the interest on indebtedness paid in 1917 by each of these corporations, not including indebtedness for purchase of obligation or securities, the interest of which was exempt from Federal income tax?

63 A. It does.

Q. Does it also show correctly the amount of the taxes paid in 1917 by each of these corporations, not including income or excess profit taxes imposed by authority of the United States or taxes assessed against local benefits?

A. It does.

Q. Now, Mr. Green, you have been, have you not, in general charge of all matters relating to the Federal income and excess profit taxes of these corporations since the first income tax law of 1909?

A. I have.

Q. And have you been familiar with all communications and relations between the United States Government and its representatives and these corporations with respect to taxes?

A. I have.

Q. And have the representatives of the Bureau of Internal Revenue from time to time examined the books and records of these corporations for the purpose of checking up their income and excess profit tax returns?

A. They have.

Q. Beginning with the year 1909 down to and including the year 1923?

A. Yes.

Q. And are you familiar with all the objections, adjustments and corrections and so forth which they have made in connection with those examinations?

A. I am.

Mr. HENDLER. I do not understand the drift of that examination.

Mr. SUMNER. I just want to show, your honor, it may not be necessary, I want to show as an additional element that the basis of allocation between income and capital has been exactly the same as the accounts on the accrual basis which the Government has approval. It is a general statement. It may not be necessary.

The COURT. It is not.

Q. In making this computation of the net income on the cash basis, it was necessary, wasn't it, to make a distinction between items of cash received and items of cash disbursed? I mean to make a distinction between capital items and income items.

A. It was.

Q. And have you used in making that distinction between capital items and income items the same system or method as you had previously used in keeping your accounts on the accrual basis?

A. I did.

Q. And have you included in the gross amount of the income received all items of cash received in 1917, which were treated on your books as income items?

A. I have.

Q. And all such items which the representatives of the Government have claimed to be income items?

A. Yes, sir.

Q. And in determining the amount of the expenses, the ordinary and necessary expenses, paid in 1917 have you included any items of cash paid other than those which were treated on your regular books of accounts as charges against income?

A. I have not.

Q. Or any items which the representatives of the Government have claimed were not proper deductions from income?

A. No.

Q. Is there any difference in determining the amount of losses actually sustained and charged off in 1917 between the accrual basis and the cash basis?

A. There is not.

Q. And you have used here exactly the same figure as was used on the accrual basis and aproved by the representatives of the Government?

A. Yes.

Q. In determining the amount of the interest on indebtedness paid and the amount of the taxes paid in 1917 have you included any items of cash which were not treated as charges against income on the regular books kept on the accrual basis?

A. No.

Q. Or any items which the representatives of the Government have claimed were not proper charges against income?

A. No.

Q. The first page of this computation, with reference to which you have been testifying, shows in a summary form, doesn't it, the net income of the American Can Company and each of its American subsidiaries separately?

A. It does.

Q. And also the consolidated net income of the American Can Company and all of its American subsidiaries determined on the cash basis?

A. Yes.

Q. And does it show the amount of dividends received by the American Can Company from domestic corporations in the year 1917?

A. Yes.

Q. Which is the same as the amount shown on the income tax return?

A. Yes.

Mr. SUMNER. I offer the computation in evidence.

Mr. HENDLER. We must object to that on the ground that it is incompetent, irrelevant and immaterial. The witness has testified that the accounts of this taxpayer were kept on the accrual basis. It appears that the return and the accounting for the year 1916 were on the accrual basis. He has further testified that the figures
66 that appear here are the same figures that appear in the account and the return on the accrual basis for the year 1917, and our position is that the taxpayer can not and is not authorized to change from the accrual to the cash basis, and therefore, that these figures are irrelevant, incompetent, and immaterial for any purpose.

The COURT. Is there any objection to this statement as showing the cash income or the income on the cash basis of the American Can Company and its American subsidiaries for the year 1917?

Mr. HENDLER. Does your honor mean is there any objection to this as representing the amounts of cash received and amounts of cash paid out?

The COURT. Yes.

Mr. HENDLER. None other than I have said before.

The COURT. Your objection goes, as I understand it, to the materiality of this proof. In other words, you say, "This is perfectly immaterial. These people have made their return upon the accrual basis and we have assessed their tax upon that basis. That is the end of their rights here. This thing is all horseplay." Now my question is, is there any dispute that this account reflects the true cash condition or the cash income condition for the year 1917?

Mr. HENDLER. As I indicated in the beginning, I am not prepared to admit that these figures are correct. I assume probably that they are, that they do correctly set out those items of cash received which

would be included in any return and items of cash paid out which would be included in any return on any basis, on either basis.

The COURT. I tell you what I will do. I understand that the books of the American Can Company are here. Mr. Green is the
67 auditor and comptroller of the American Can Company and the auditor of the other companies. If you want to have this thing checked over in any way with the books of the concern, we will take a longer recess so that they may be done. We will take a recess until two o'clock. If, however, you do not desire to cross-examine after that examination it may be marked in evidence. Of course, it may be marked in evidence possibly even after your cross-examination. I will reserve that question. On the question of the immateriality of the statement, I will overrule your objection and allow an exception.

Defendant's counsel prays an exception, which is hereby allowed and sealed accordingly.

[Sealed.] J. L. BODINE.

Mr. HENDLER. Mr. Crawford from the United States attorney's office in New York just advised me that under some arrangement that has been at least tentatively, if not definitely entered into there, there are going to be several weeks allowed for the checking over. Now, it may be possible that during the noon recess some arrangement substantially the same as that entered into in New York may be entered into which may simplify the entire matter for your honor and everybody concerned.

Q. Mr. Green, are the books and records of the American Can Company and its subsidiary companies, which were used in making this computation of the income for the year 1917 on the cash basis, here in the court room?

A. They are.

Q. Except for certain vouchers sustaining the cash payment which I understand are loaded on a truck which stands on the street now at the door of the courthouse?

68 A. Yes.

Mr. SUMNER. I would like to state on the record, your honor, that all these books and records are available for examination by the defendant.

I will ask to have the computation of the net income on the cash basis with respect to which the witness has testified marked for identification.

(Received and marked "P–7 for identification.")

The COURT. We will take a recess now, gentlemen, until two o'clock

AFTER RECESS

The COURT. Counsel for the Government requests that they may have a reasonable opportunity to examine the books and vouchers

of the American Can Company and its American subsidiaries with a view to checking the correctness of the statement contained in the plaintiffs' Exhibit P–7. Mr. Sumner does not oppose this application, so long as a reasonable time is alloted for that purpose. The exhibit will be marked in evidence, subject to correction by the Government and subject to motion to exclude if material inaccuracies appear therein.

(Exhibit P–7 for identification received and marked "Exhibit P–7.")

The COURT. Now it is only a question of time which the Government should have, two weeks or three weeks.

Mr. SUMNER. My experience in these things is that unless a fairly limited time is fixed it does not get done.

The COURT. Suppose we have it this way. February 12th is Lincoln's Birthday and February 22d is Washington's Birthday. I think they ought to be in a position to say whether this thing
69 is right or wrong before the birthday of one or the other of these patriots. I take it that Washington's Birthday being more remote they will choose Washington's.

Mr. SUMNER. As I understand the case now is fixed for February 21st.

The COURT. That is the time they are going to make the statement as to this account, this Exhibit P–7. Now, after the testimony is closed finally, I suppose that the case will have to be argued some day. We can have it argued almost any time that you want, but I do not suppose until these questions are definitely settled that you will want to prepare a brief. You may exchange briefs and then argue the case after the exchange of briefs.

Mr. HENDLER. And if it should develop that it is necessary to cross-examine as to some of the items we can have the witnesses back for that.

Mr. SUMNER. Surely. I think that we ought to have a day fixed.

Mr. HENDLER. Yes; I would arrange with you for that.

The COURT. Now, Counselor, Mr. Starr, Mr. McNichol, and Mr. Essler have been witnesses sworn in this case. This statement is made up from information which they procured for this witness. Do you desire they should be put on the witness stand to testify to those facts?

Mr. HENDLER. No; with the same understanding that if it developed I should have to ask them a question or two on cross-examination that I may have an opportunity to do so.

Mr. SUMNER. I will produce these witnesses for the Government.

The COURT. Their formal testimony is waived and their testimony on direct examination is then waived. Now, that is your case?
70 Mr. SUMNER. Except for the calculation of the taxes. Do you think that it would be better to let that wait until the facts are finally established?

The COURT. Is this witness a tax expert?

Mr. SUMNER. Mr. Green is. He is the one that made the calculation.

The COURT. You may offer Mr. Green's calculation in evidence as P–8, subject to the same corrections and the same cross-examination if necessary.

Mr. SUMNER. I will just ask him one question.

CHARLES E. GREEN resumes the stand.

Direct examination by Mr. SUMNER:

Q. Mr. Green, did you make this calculation of the amount of the taxes, the amount of the income and excess-profit tax payable by the American Can Company, the Missouri Can Company, and the Detroit Can Company on the basis of the net incomes shown in plaintiffs' Exhibit P–7?

A. I did.

Q. In accordance with the provisions of the revenue act of 1917?

A. Yes, sir.

Q. And that is a correct calculation?

A. It is.

Mr. SUMNER. I offer it as your honor suggested. Of course, it is only mathematics you know.

(Received and marked "Exhibit P–8.")

Just one more general question.

Q. Have any of the taxes which are claimed in these suits been refunded to the plaintiffs by the defendant?

A. They have not.

Q. Have any part of them been credited to the plain-
71 tiffs or any of them as against other Federal taxes payable?

A. They have not.

Mr. SUMNER. I think that is our case, your honor.

May I say in explanation that the figures shown on this plaintiff's Exhibit P–8 as the amounts of the taxes paid prior to March 7, 1921, in the case of the American Can Company represents totals of the payment which was proved in evidence and the subsequent payments which are alleged in the complaint and admitted in the answer. In other words, these statements, plaintiffs' P–8, show the total amount of taxes paid prior to March 7, 1921, to Edwards, collector, and they include the amounts which were paid on or about June 14, 1918, as established by evidence this morning and amounts which were subsequently paid by the American Can Company as alleged in the petition and admitted in the answer and not covered by the evidence, but, of course, being admitted by the answer the evidence is not necessary.

Mr. HENDLER. I do not know whether it clearly appears here, but I think this correctly states the matter; that these three suits here are for the recovery back of taxes, or a portion of the taxes that were paid as shown by their return. Is not that correct?

Mr. SUMNER. To some extent; yes.

Mr. HENDLER. You are not suing in these three proceedings, as I understand it, to recover anything that was an additional assessment.

Mr. SUMNER. Yes.

Mr. HENDLER. I thought all of those additional assessments were paid to Collector Bowers.

72 Mr. SUMNER. No, the petition sets that out quite fully. The American Can Company paid three million odd dollars of taxes in 1918 at the time or soon after filing the return. Then subsequent to that and prior to March, 1921, the commissioner made an additional assessment against the American Can Company for additional taxes, $1,900,000.00, which is alleged in the complaint and admitted in the answer. That was both invest'd capital and income, but for those amounts, that subsequent amount of $1,900,000 an additional assessment was made. But the total amount claimed in this suit being about two million dollars includes the $1,900,000 and a part of the amount which was paid in 1918.

Mr. HENDLER. There is no question involved in this case about the adjustment of invested capital that was arrived at?

Mr. SUMNER. We understood there is no question of invested capital here; we are using the figures for invested capital which the commissioner finally determined.

Mr. HENDLER. Yes; that is what I understood.

The COURT. The clear issue is whether this return should have been made on a cash basis for this year after all the things had happened that did happen.

Mr. SUMNER. Yes. There is a possible intermediate point, but I do not think it is worth going into now even if your honor should hold that we could not go back to the cash basis or back of the original return there would be this additional income which was added on after the return. There would be about six hundred thousand dollars of this amount in any event, it seems to me, recoverable as that was tax on income that the commissioner added after our return. In other words, we are going back—we argue first we

73 have the right to go back and pay tax on the amount of income that the revenue act said we were obliged to pay taxes on and nothing more, in view of the fact that the amount we returned was in excess of that and the commissioner has rejected that figure in saying that the basis was not proper.

Mr. HENDLER. So far as paying the tax the statute says they should have paid, there is no difference between counsel and ourselves. The difficulty is that he reads the statute one way and I read it another, which frequently happens among lawyers.

The COURT. That is all going to be simplified when the law is restated by the Harvard Law School.

Mr. HENDLER. My attention is directed to the fact that possibly I should reserve an exception to the admission in evidence of these papers on the theory that I stated this morning.

The COURT. I think, Counselor, that you are entitled to that, but you already had it.

Mr. HENDLER. I had it as to the one, but not the others, and I would like to reserve it as to both.

The COURT. Yes.

74 In United States District Court

AMERICAN CAN COMPANY, MISSOURI CAN COMPANY, AND DETROIT CAN COMPANY, plaintiffs

vs.

THE UNITED STATES, DEFENDANT

Bill of Exceptions

Filed November 9, 1927

Transcript of proceedings taken at Trenton, N. J., before Hon. Joseph L. Bodine, D. J., on May 16, 1927.

Appearances: John J. Treacy, Esq.; Graham Sumner, Esq., for the plaintiffs; Walter G. Winne, Esq., U. S. Attorney; Charles T. Hendler, Esq., Special Attorney, Internal Revenue, for the United States.

Colloquy between court and counsel

Mr. SUMNER. If your honor please, it has been some time since we were together. I do not know whether this matter is still fresh in your honor's mind.

The COURT. It is a matter to recover excess income tax predicated upon a difference in bookkeeping systems between you and the Government.

Mr. SUMNER. Yes.

The COURT. What more should I know about it?

Mr. SUMNER. The claim made by the plaintiff in this suit is that their Federal taxes for 1917 should be computed on the amounts of their income for that year determined on the cash basis as defined in section 12 of the revenue act for that year, and if they were so
75 determined the amounts which they had already paid would exceed very largely the amounts which were properly payable. And your honor will recollect at the close of the last hearing we offered in evidence a computation which had been made by the comptroller or auditor of the plaintiff to show the amount of the net income on the cash basis, and your honor admitted it subject to correction by the Government, and the Government asked for a

reasonable time in which to check the books and records of the plaintiff and so forth, which, was allowed.

Now, since then the representatives of the Government have examined the books and records of the plaintiff and have made a report, a copy of which I understand was sent to your honor and another copy was sent to us, and, as I understand it, from that report there is really no dispute with respect to any figures except for two items amounting to about $81,000; that is, as I understand the report, the Government auditors take the position that all the figures which were included in the computation which was admitted in evidence as Exhibit P–7 are correct, except for the amount of the losses of the American Can Company, and that it is claimed that the amount of the losses of the American Can Company are stated at about $81,000 too much.

Now, I suppose the first thing here this morning is to just get exactly clear what the issue is as between the Government and the plaintiffs.

The COURT. What is the use of bothering about that figure of $81,000?

Mr. SUMNER. If that is the only point, I will not spend two minutes on it. We will waive it. I mean, I am perfectly prepared if that is the only thing in dispute here to correct the computation we put in before to that extent. And if I am correct in understanding that except for that correction the Government concedes our
76 computation is correct as made under section 12 of the Revenue Act of 1917——

Mr. HENDLER. We do not concede that. Of course, if we did we would concede the case. Now what we are willing to concede, if your honor please, is this. In the first place I did not understand when we separated that those two statements had been received in evidence. My understanding was that that itself was open. However, what we concede is that the figures that are shown in that statement are supported by the books of the plaintiff, except with regard, I think, there were two items, one relating to interest on Liberty bonds, which we understood at the time had been conceded by the gentlemen of the American Can Company, and the other was a deduction for bad debts, which I understand now Mr. Sumner to concede this morning. That is as much as we can concede this morning with regard to the statement, except conceding ourselves out of court.

The COURT. Correct the statement by the elimination of $81,000 loss on bad debts.

Mr. SUMNER. Then, do I understand that if that correction is made, Mr. Hendler, this statement shows correctly the gross income received and the expenses?

Mr. HENDLER. Do not ask me to go into detail about that.

The COURT. Mr. Sumner, if the thing goes in evidence with those two corrections and it is conceded that the books support that state-

ment, then any conclusions from those statements are a matter of law which the court may make or any other court may make.

Mr. SUMNER. Then, suppose I offer in evidence, or I will state on the record that the plaintiffs are willing to concede the two corrections which the Government desires to make with respect to the figures shown in Exhibit P–7, consisting of two items included in the losses of the American Can Company aggregating $81,526.26,
77 the effect of which is to increase the amount of the income of the American Can Company and the consolidated income of the American Can Company and its American subsidiaries determined on the cash basis to the same extent, and in order to make the correction I will offer in evidence two papers to be substituted for the first two pages in Exhibit P–7, the only two pages which are affected by that change, which I think, if received in evidence, will show the effect of these changes and the exact amount of the income of the American Can Company and its American subsidiaries, and its consolidated income.

Mr. HENDLER. Well, I would like to look at the figures.

Now, of course, if your honor please, in making our concession as to those figures we do not want to be understood as conceding that these statements, or any part of them, are admissible for any purpose in this case. In other words, our position is that they are immaterial, irrelevant, and incompetent. We are not objecting to the method of proof, as your honor understands, but if the witnesses were asked these questions separately we would object to them for this reason, if for no other, that if the purpose in introducing those questions is to change the method upon which the books of this corporation were kept and upon which its income-tax returns were thereafter and for the year in question made, then we object to it as irrelevant, incompetent, and immaterial.

The COURT. Objection overruled.

Mr. HENDLER. And your honor will allow us an exception?

Exception allowed.

[Sealed.] J. L. BODINE.

Mr. SUMNER. I offer this. There are two pages.

(Received and marked "Exhibits P–9 and P–9a.")

78 Mr. SUMNER. There are just two techincal questions I would like to ask Mr. Green, and then Mr. Hendler wishes to cross-examine.

CHARLES E. GREEN, called and having been previously sworn, testified as follows:

Direct examination by Mr. SUMNER:

Q. Mr. Green, I show you Exhibit P–7, which was admitted in evidence at the last hearing and with respect to which you gave testimony which purports to show the income of the American Can Company and its American subsidiaries determined upon the cash basis for the year 1917, containing the gross income received and

the amounts of the expenses, losses, taxes, and interest as defined in section 12 of the act. Now, in making that computation, Mr. Green, were there included in the figures for the ordinary and necessary expenses any items representing rentals or other payments required to be made as a condition to the continued use or the possession of property to which the American Can Company, or any of its American subsidiaries, had taken or were taking title or in which any of them had an equity?

A. No.

Q. In the computation of the amounts of interest on indebtedness paid in 1917 by each of these corporations, were any amounts of interest included upon indebtedness which in any case exceeded the amount of the paid-up capital stock of the corporation in question outstanding at the close of the year?

A. No.

Q. And in making the computation of the taxes paid in 1917, were any amounts included other than taxes imposed by the authority of the United States, or of its Territories or possessions, or any foreign country, or by the authority of a State, county, school district, or municipality, or other taxing subdivision of any State?

A. No.

79 Mr. SUMNER. There are two or three limitations in the definition of the act. I just wanted to show that we came within them. Then I shall put in another computation.

Q. Mr. Green, have you made another computation of the taxes payable by the American Can Company for 1917, based upon the income determined on the cash basis as revised this morning and shown on Exhibit P-9?

A. Yes.

Q. Is this paper which I show you the computation which you made?

A. Yes.

Q. And that computation is based upon the consolidated invested capital as fixed in the commissioner's letter of March 7, 1921, and on the income determined on the cash basis as shown in Exhibit P-9?

A. Yes.

Q. And it includes both excess-profit tax payable by the American Can Company in behalf of itself and all its subsidiaries and income tax payable by the American Can Company on its own income?

A. It does.

Mr. SUMNER. I offer it in evidence. This is to take into account the correction of the income we made this morning. It is all mathematics. I suppose it might be taken subject to correction.

Mr. HENDLER. We have no objection, except that which has been already stated as to the entire paper.

The COURT. As to its competency?

Mr. HENDLER. Yes, and its relevancy.

(Received and marked "Exhibit P–10.")
Exception allowed.
[Sealed.] J. L. BODINE.

80 Q. Have you made another computation of the Federal taxes for 1917 which would be payable by the American Can Company and its American subsidiaries based upon their net incomes as returned?

A. Yes.

Q. Are these two papers, which I show you, the computation which you so made?

A. They are.

Q. And that computation is based on the consolidated invested capital as fixed in the commissioner's letter of March 7, 1921, and the income of the American Can Company and its various American subsidiaries as returned?

A. It is.

Mr. SUMNER. I offer the paper in evidence.

Mr. HENDLER. I did not get that.

Mr. SUMNER. I will state the only purpose of this is—there are really two bites in this case, one is with respect to the increase in the income which the commissioner made over and above the amounts of the income as returned by these companies. The other theory is we have a right to go back and claim income even below the amounts returned, but in order to make the complete record it seems to me this computation should be put in for what it is worth. This computation is based on the amounts of the income of these various companies as shown in their returns, as filed, and upon the amount of the invested capital as determined in the commissioner's letter of March 7, 1921. It shows an overpayment by the American Can Company of about $620,000.

Mr. HENDLER. Subject to the same objection and exception and the privilege of checking up and seeing whether it is in accordance——

The COURT. The objection is to the relevancy?

81 Mr. HENDLER. Yes.

The COURT. Not the method of proof?

Mr. HENDLER. No.

The COURT. And is taken subject to your right to correct. All right, let it be marked.

Exception allowed.

[Sealed.] J. L. BODINE.

(Received and marked "Exhibit P–11.")

Mr. HENDLER. May I have a copy of that, Mr. Sumner?

Mr. SUMNER. Yes.

Cross-examination by Mr. HENDLER:

Q. Mr. Green, the American Can Company and its subsidiaries have always kept their books on the accrual basis, haven't they?

A. They have.

Q. They made their returns for income taxes for the year 1916 on the accrual basis, didn't they?

A. They did.

Q. And they made their return for income taxes for the year 1917 on the accrual basis?

A. They did.

Q. And that is true of 1918, too, is it not?

A. Yes.

Q. Now when was this so-called inventory constant account set up on the books of the company?

A. In January, 1917.

Q. What time in January?

A. The account was started the first of January, and at the close of January my recollection is that the transfer was made.

Mr. SUMNER. I am going to interpose an objection to the materiality and relevancy of this evidence. Maybe your honor
82 will wish to take it all, but I would like to note an objection on the record. It seems to me to be immaterial to go into the details of this inventory matter, in view of the fact that the commissioner has ruled and determined practically for all purposes in these suits, that the basis on which the books were kept and the return was made did not clearly reflect the income. It does not seem to me to be material to go into the details as to whether it did or not, or what the method of procedure was which the company actually followed. It is a question, I suppose, whether your honor thinks it wiser to take it all now or not.

The COURT. I think I will take it now subject to your objection.

Mr. SUMNER. May I have my objection and exception noted then?

The COURT. Yes.

Exception allowed.

[Sealed.] J. L. BODINE.

Q. In other words, this was determined to be done on the last day of January, was it?

A. Yes.

Q. And the account dated back to the first of January?

A. Yes.

Mr. SUMNER. Same objection.

Mr. HENDLER. You need not repeat that. It will be understood that your objection will go to all of it, Mr. Sumner.

Mr. SUMNER. Very well. Thank you. Sometimes in New York we consider we have to repeat it right along in order to make the record.

Mr. HENDLER. I have had judges hold me down for doing it and tell me one exception was as good as one thousand.

83 Mr. SUMNER. We have a habit of whispering to the stenographer, "Same objection and same exception," just to complete the record.

Q. When was it determined at the meeting of the directors that that course would be pursued?

A. I know nothing about the meeting of the directors.

Q. Wasn't it determined at a meeting of the board of directors?

A. Not as far as I know.

Q. Who determined it?

A. The president of the company gave me instructions.

Q. When?

A. Shortly after the first of the year.

Q. What connection was there then in your answer as to the latter part of the year and the first of the year?

A. Because it was necessary to consider the inventory of December 31, 1916, and the purchases during January, 1917, that is the transactions during January which went to make up the final transfer item, which was made at the close of January.

Q. Well, now will you please explain just what was done with that inventory constant account. How it was handled?

A. The inventory constant account was the result of writing up the value of the December 31, 1916, inventory of tin plate from a $3.60 per base box to $7 per base box, and writing up all of the purchases that were received after January 1st from $3.60 per base box to $7, and then at the close of January transferring from that write up account to an inventory constant account.

Q. What was the value then?

A. Well, it was $6,250,000 for the American Can Company and all of its subsidiaries, including one of the Canadian subsidiaries, which is, of course, not included in any of these calculations.

Q. Was that as of January 1, 1917? Did that then
84 represent the actual amount of tin on hand and in process?

A. My recollection is that on January 1, 1917, there was not 1,800,000 base boxes on hand.

Q. Have you any means of determining that readily?

A. I have not any papers here.

Q. Mr. Green, I show you a statement that was prepared. Were not those figures showing the inventories at the beginning of the year and at the end of the year submitted to the Government auditor by your office?

A. There were such figures submitted.

Q. Have you any means of determining whether that paper truly shows the figures that were submitted by your office?

A. I have not any figures here that would enable me to do that.

Mr. SUMNER. These seem to be correct. They are made up from a statement which we furnished the Government. I think there should be a notation on this statement between "a" and "b", however. Do you want to offer this in evidence?

Mr. HENDLER. I have not determined yet.

Mr. SUMNER. The only thing I note is that the meaning of these two lists of figures is not explained. One is the total for department A and the other for department B.

Mr. HENDLER. In this statement, I believe it is marked "P-7," was there any account taken of inventories at all?

A. There was not.

Q. Would it be possible to show the income of the American Can Company by wholly disregarding the opening inventory, which was the closing inventory in your return of 1916, and deducting the inventory of the goods on hand and in process at the close of 1917?

A. It would be on a cash receipt and disbursement basis.

85 Q. Then if the American Can Company during the year 1917 had invested all of its earnings in real estate, let us say, could you show the income of the American Can Company without taking into account the value of the real estate in which its earnings had been invested during the year?

A. No.

Q. Well, could you, assuming now that all of the earnings of the American Can Company had been invested in raw material during the year 1917?

Mr. SUMNER. I am going to make another objection on the ground that this is immaterial, irrelevant, and incompetent in view of the fact that the section of the revenue act of 1917 under 12a definitely defines the method for determining income on the cash basis, and that the question as to how it should be done, whether inventories should be used or should not is really a question of law. That section says in so many words that the income is to be ascertained by taking first the gross amount of the income received within the year and deducting therefrom expenses of maintenance and operation, losses actually sustained and charged up, taxes paid and interest paid on indebtedness. It is a very definite mathematical formula. It says not a word about inventories or accounts receivable, and the courts have ruled repeatedly that that formula means cash received less cash paid, except for the item of losses which is the only non-cash item, and as soon as you get into inventories or accounts receivable or accounts payable you get away from the cash basis and you bring into the calculation certain factors which are not authorized or included within section 12 of the act. It seems to me that Mr. Hendler is now getting

86 right on to a question of law rather than one of fact as to what this witness may know or may not know, and, of course, this point is one that your honor is about to consider sooner or later, and I would be very glad if your honor thinks this is the right time to direct your attention specifically to the exact words of that section of the statute, because what we are trying to do here is to deliberately figure the income in accordance with that section of the statute literally as Congress provided it should be done.

It is not a question of what accountants may think is the right way or best way to determine income or the way business men may think

It is a question of following out a definite edict of Congress, and I have that statute right here.

Mr. HENDLER. Well, it seems to me that my friend is seeking to argue a point which will have to be argued at length.

The COURT. It seems to me you were arguing the point of the witness, Mr. Hendler.

Mr. HENDLER. No; your honor.

The COURT. This witness is a fact witness as to what the books show. Now, of course, cross-examination is open to you if his concise statements were incorrect in any way. But it occurred to me it was conceded they were not.

Mr. HENDLER. No. I think that Mr. Sumner's examination of this witness in qualifying him and leading up to the introduction of that statement was along the lines of an expert. I may be in error, but my recollection is that the direct question was put to this witness whether this statement correctly reflected the income of the American Can Company and its subsidiaries.

Mr. SUMNER. No; the question put to this witness was solely to prove the facts and figures falling within the five groups defined in the statute. I did not ask him whether in his opinion that
87 was the right way of determining the income. It seems to me all discussion as to whether it is possible to do it in this way and so forth along the line that Mr. Hendler is now asking is beside the point and really involving a question of law.

Mr. HENDLER. Now I think this question permits me to go into this proposition. The witness has testified this morning that their system of accounting was the accrual system, and that it always has been; that their system of making their income tax returns both prior to, for the particular year in question, and for subsequent years was on the accrual basis. Now I think we are entitled to show from this witness—I may be in error about that—but it seems to me there is somewhere here, I can not just lay my finger on it, a question or two which apparently was intended to qualify this gentleman as an expert accountant.

Mr. SUMNER. I will concede that he is an expert accountant.

Mr. HENDLER. And if there is such a question then I am entitled to cross-examine along the line that I have indicated here now.

The COURT. Does not this case resolve itself down into a very simple compass? Conceding that the books were at one time kept upon an accrual basis.

Mr. HENDLER. The witness has testified that they always have been and are now.

The COURT. Then comes the question of keeping the books on a cash basis. That is, the claim is that they are entitled to pay income tax on the cash basis.

Mr. SUMNER. We are not bound by our books, your honor.

88 The COURT. I understand that, Mr. Sumner, but the basis of your contention is that you are entitled to pay on the cash basis, and you have introduced facts and figures to show what that

income was on the cash basis. Now, that is all this witness has in chief testified to.

Now, why should we ask him what is the best method or what method more truly reflects income? You can argue that, Mr. Hendler, with the United States Senators and Congressmen. That is the basis of the statute they passed. They went into it at great length to show which or both or what method reflected income. It is entirely academic.

Mr. HENDLER. I submit it is not, not the point I make.

The COURT. Well, I sustain the objection to that question.

Exception noted.

[Sealed.] J. L. BODINE.

Q. Mr. Green, in making your statement—let me first ask you whether you did not in making the return for 1916 include in your income tax return for that year made on the accrual basis, bills payable as an accrual item?

A. Yes.

Mr. SUMNER. That is objected to as immaterial, irrelevant, and incompetent. I do not see how that has anything to do with this case, what they did in 1916 or what they did not.

The COURT. I will allow that.

Mr. SUMNER. I note an exception.

Q. When you came to change from the accrual basis on which you made your return in 1917, did you do anything towards reconciling those accrual figures from your 1916 return?

A. No, sir.

89 Q. There was nothing of that kind done?

A. No.

Q. In other words, as I understand it, and I am not trying to hide anything away from you, no attention was paid to those items, deduction for which had been taken on the accrual basis in your 1916 return in this statement?

Mr. SUMNER. I repeat the objection that it is irrelevant, incompetent, and immaterial. It comes right back to the question of following the definition laid down by Congress. They say how to determine income, and we have tried to follow it.

Mr. HENDLER. I do not concede that for a minute. This statute under which these returns were made and under which this lawsuit grows is an income tax statute and Congress——

The COURT. I did not sustain the objection.

Mr. HENDLER. Oh, I beg your honor's pardon. I thought you had indicated—or at least had not indicated which way you were about to rule.

The COURT. I did not have an opportunity to.

Mr. HENDLER. I have always thought that where an objection is made and no remarks made it was sustained.

The COURT. Let us get along.

Mr. SUMNER. Did your honor overrule my objection?

The COURT. Yes.

Mr. SUMNER. May I have an exception?

The WITNESS. Repeat the question, please.

Q. (Question repeated by stenographer.)

A. No, there was no adjustment made of such items.

Q. And I may have asked you this, but out of an abundance of caution I will ask it again. In this statement which has been submitted to the court, there is no mention made of any amount of raw tin on hand on December 31, 1917, is there?

90 A. No.

Q. Now, Mr. Green, have you anything present that will show the amount of tin on hand and in process on the 1st of January, 1917?

A. I have not in my possession now.

Mr. HENDLER. If your honor will please indulge me a minute, I think we are really saving time while I will look over this paper.

Q. Mr. Green, I show you a statement which was evidently prepared in your office, which shows the quantity and cost of tin on hand and in process on the 1st of January, 1917, and the quantity of tin purchased at $3.60 a box that was delivered in 1917, and the quantity of tin purchased during 1917 at $7 a box, and the quantity of tin on hand and in process on December 31, 1917. Are those figures correct?

A. Yes.

Q. They are taken from your books?

A. They are.

Mr. HENDLER. I offer that in evidence.

Mr. SUMNER. It is objected to on the ground that it is immaterial and irrelevant on the issues of the case. Of course, we do not question the figures.

The COURT. It may be received in evidence.

Mr. SUMNER. Exception.

(Received and marked "Exhibit D–1.")

The COURT. I might say except where I refuse an exception the stenographer always writes them up.

Mr. HENDLER. What I was about to say now was a more general proposition than that. I do not want to consume time needlessly. I was about to develop from this witness the fact as to whether this statement as prepared and offered in evidence reflected the true income of this corporation.

91 The COURT. Mr. Hendler, what is income is a matter of debate between accountants, bookkeepers, and what not, and, therefore, Congress defined in its statute what income is; that is receipts from different sources. Now, all I am excluding from you is with respect to the academic side of the matter as to what income is. You may inquire to your heart's delight as to this particular statement and the facts and figures therein shown.

Mr. HENDLER. I think as narrowed to that proposition I have asked very nearly everything. Of course, as to the figures themselves we have indicated there is no difference between counsel. What I had proposed to develop, and I may save the entire exception by one question I will propound to the witness, and that is whether, having kept your books of account on the accrual basis, and having made your returns for the years 1916, 1917, and 1918 on the accrual basis, the so-called cash receipts and disbursement basis, without taking into account the opening and closing inventories for the year 1917, would it correctly reflect the income of the American Can Company during the year 1917?

Mr. SUMNER. That is objected to as irrelevant, incompetent, and immaterial for the reasons stated before.

The COURT. It seems so to me.

Mr. HENDLER. Well, I think your honor will allow me an exception. We have no further questions to ask this witness.

Exception allowed.

[Sealed.] J. L. BODINE.

92 Redirect examination by Mr. SUMNER:

Q. Just one question. You said something about the stock of tin plate on hand at the beginning of 1917 being less than 1,800,000 boxes.

A. Yes.

Q. Were the stocks at that time lower than usual?

A. Yes; they were.

Q. They were considerably lower at the beginning of 1917 than at the beginning of 1916?

A. Yes.

Q. Several hundred thousand boxes less?

A. Fully that in my recollection.

Q. That would indicate the business in 1916 had consumed all that were purchased that year and in addition some of the stock which had been on hand?

A. Yes.

Recross-examination by Mr. HENDLER:

Q. There was one question in connection with a question Mr. Sumner asked you, which I would like to ask. There were some purchases in 1916 that were not delivered until 1917?

A. Yes.

Q. Until after the first of January?

A. Yes.

Mr. HENDLER. That is all.

Mr. SUMNER. If your honor please, the plaintiffs rest.

93 DEFENDANT PROOFS

HERBERT POTTHOFF, called and sworn as a witness in behalf of the defendant, testified as follows:

Direct examination by Mr. HENDLER:

Q. Mr. Potthoff, what is your business?

A. I am an auditor with the Income Tax Unit of the Internal Revenue.

Q. Did you take any course of study anywhere to prepare yourself as an accountant?

A. I have.

Q. Have you any degree?

A. No commercial degree; no.

Q. Where did you study?

A. Pace Institute.

Q. How long have you been connected with the auditing force of the Internal Revenue Bureau?

A. About five years. No; more than that—seven years.

Q. And in that connection how wide has your experience been?

A. Well, it has extended over every class of corporation and practically over every State in the Union.

Q. And hundreds of corporations, I assume?

A. Yes.

Q. And that involved going into their accounting methods?

A. Yes.

Q. And you were one of the auditors who checked these books?

A. I was.

Mr. HENDLER. As an accountant do you assume that he is qualified to testify as an expert?

Mr. SUMNER. I should suppose that he was as an accountant; yes.

94 Mr. HENDLER. I am not asking him as a lawyer.

Mr. SUMNER. I do not know what you are going to ask him.

Mr. HENDLER. I am going to ask him the questions that I tried to get Mr. Green to answer.

Q. Mr. Potthoff, where a corporation keeps its books on the accrual basis, has always kept its books on the accrual basis, and has made its income-tax returns on the accrual basis, both before and after the year in question and in fact made its return for that year on the accrual basis, with that system of accounting and reporting is it possible to reflect the income of the corporation for the taxable year without taking into account the opening inventory at the beginning of the year and the closing inventory at the end of the year, in your opinion?

A. No; it is not.

Mr. SUMNER. May I have the objection noted before the answer?

Mr. HENDLER. I will make no point of that

Mr. SUMNER. As immaterial and incompetent, on the same grounds as stated before.

The COURT. Also as not a matter of expert testimony.

Mr. SUMNER. This witness is not qualified to answer the question; put it that way.

The COURT. The answer may stand and you may have your exception.

Q. Now, along that line, Mr. Potthoff, if a man begins business on the 1st of January, 1917, and deposited in bank say $10,000 and purchased during the year 1917 raw materials to the amount of $10,000 and manufactured and sold all of those raw materials purchased during the year for $25,000 and had on hand raw materials at the end of the year amounting to $10,000, what, having in mind your former answer, would the income of that individual be for that year?

95 Mr. SUMNER. I object as irrelevant, incompetent, and immaterial for the reasons I have previously stated. It is purely hypothetical and has nothing to do with this case and involves a question of law and opinion, which are not material and which Congress passed upon and which this witness is not qualified to answer.

The COURT. I will allow an exception.

A. Well, without stating an amount, I would say inventories would have to be taken into consideration to determine the proper inventory.

Q. But I have given you the inventory statement $10,000. He owes nothing and has no bills receivable.

The COURT. And he has no money in the bank.

Mr. HENDLER. He has no money in the bank.

The COURT. May be he owes some money. I do not know.

Mr. HENDLER. No; I say that he owes nothing and has no bills receivable.

The COURT. I can answer that his income is $25,000, and I do not have to be an expert.

The WITNESS. I would say $25,000.

The COURT. He certainly has been a very fortunate man. I would like to be able to engage in that kind of business myself.

Mr. HENDLER. I only took those figures, your honor, because I thought they would be readily taken in as we went along.

Q. Mr. Potthoff, in making this audit based upon the figures as you saw them in the books of the plaintiff, did you make up a detailed statement based on the ruling by the commissioner assessing the additional taxes against the plaintiff?

A. Yes.

Q. Have you a copy of that?

A. Yes [paper handed to counsel].

96 Q. This statement was not among the papers that were submitted to his honor and counsel on the other side?

A. No.

The COURT. I have never had any papers submitted to me.

Mr. HENDLER. It was sent to the United States Attorney, your honor under our agreement.

The COURT. Well, that does not prove that I had them.

Mr. HENDLER. No; I can only prove by that statement that I did what I contracted to do.

The COURT. There is no trouble about having this admitted, is there, except to its relevancy.

Mr. SUMNER. I have never seen it before until this morning, and I do not know what is in it. If their meaning is clear——

The COURT. I understand they are. The figures show the way in which the commissioner made his assessment of taxes.

Mr. SUMNER. I have no objection except that it is immaterial and irrelevant. But I have not had a chance to look at this. If your honor will allow me about two minutes.

Q. You also made up a statement, did you not, in more detail based upon the return as originally filed by the plaintiff corporation and its subsidiaries?

A. Yes.

Mr. HENDLER. We offer those two statements in evidence, the first marked statement showing "Consolidated net income" as reported on return, and the other marked "Statement showing consolidated net income as amended."

Mr. SUMNER. And that means as amended by the Commissioner of Internal Revenue and shown in the letter of March 7, 1921?

The WITNESS. That is right.

97 Mr. SUMNER. Objected to as immaterial and irrelevant.

The COURT. It may be marked subject to an exception.

(Received and marked "Exhibit D–2 and D–3.")

Q. Then did you also make up an comparative statement based upon the claim as made by the plaintiff here on the cash receipts and disbursements basis without the use of inventories and with the use of inventories shown in the same statement?

A. Yes.

Q. This, I understand, was already furnished to counsel for the plaintiff?

A. That is correct.

Mr. HENDLER. We offer that statement in evidence.

Mr. SUMNER. That is objected to as irrelevant, incompetent, and immaterial, and it does not seem to me that it ought to be admitted. In the first place, the method by which it was prepared is not shown clearly enough to enable anybody to know what the figures mean.

The COURT. What is the purpose of it anyway? It is a comparison of two methods, isn't it?

Mr. HENDLER. I would not say two methods. Well, it would probably be designated that way, one with and one without.

The COURT. You see, Mr. Hendler, the issue in this case is, should this return have been made as the plaintiffs contend the statute reads. Your contention is that it should have been made up as the commissioner ruled that it should be. This does not seem to me to be helpful at all.

Mr. HENDLER. I feel that in this case we should be permitted to show—I may be wrong on that—but I think that we should
98 be permitted to show that even granted that the plaintiff under the statute was permitted to make its return on the cash receipts and disbursement basis that even though that were done substantially the same figure would be arrived at by what we contend would be the correct method, particularly in a large manufacturing corporation like this, including inventories.

Mr. SUMNER. The chief difficulty is that the method which has been followed here comes out of the mind of the witness. It is not in the statute.

The COURT. It seems to me that I am going to exclude this for that very reason. I have to cut the proofs down somewhat for the sake of saving cross-examination in the opening up of a new subject matter. Now it seems to me that this opens up new subject matter.

Mr. SUMNER. It certainly does.

The COURT. I have let your witness show that it is proper to include that question of inventory in the cash basis, whereas I did not permit that question on cross-examination. I do not think it is properly in the case, but I let it go in, and I think on taking this I opened the door to a lot of irrelevant matter. If I am wrong I will be straightened out. Let it be marked for identification.

Mr. HENDLER. And excluded and an exception noted.

The COURT. Yes.

[Sealed.] J. L. BODINE.

(Received and marked "D–4 for identification.")

Mr. HENDLER. Now we have the other gentleman here who assisted in this.

The COURT. It is conceded if called he would corroborate this witness on the point on which he has already testified.

99 Mr. HENDLER. Yes; I am willing to concede that, except to the same objection as to its relevancy and competency.

The COURT. That is your case?

Mr. HENDLER. Yes.

The COURT. Now, gentlemen, when do you want to argue this case?

Mr. SUMNER. We are here. Would it be feasible to do it this afternoon?

The COURT. Perfectly. I question whether or not it will be very effective, as it is a question after all to be thoroughly covered in the briefs.

Mr. SUMNER. Yes; I think so. The record is very simple.

The COURT. Yes; but it is a matter of very close reasoning, and I suppose a good deal of time can be saved by having it well briefed.

Mr. SUMNER. If you think the argument would be a help, I will be glad to go on this afternoon.

The COURT. What I would like to do is to have printed briefs and have the argument given from the printed briefs.

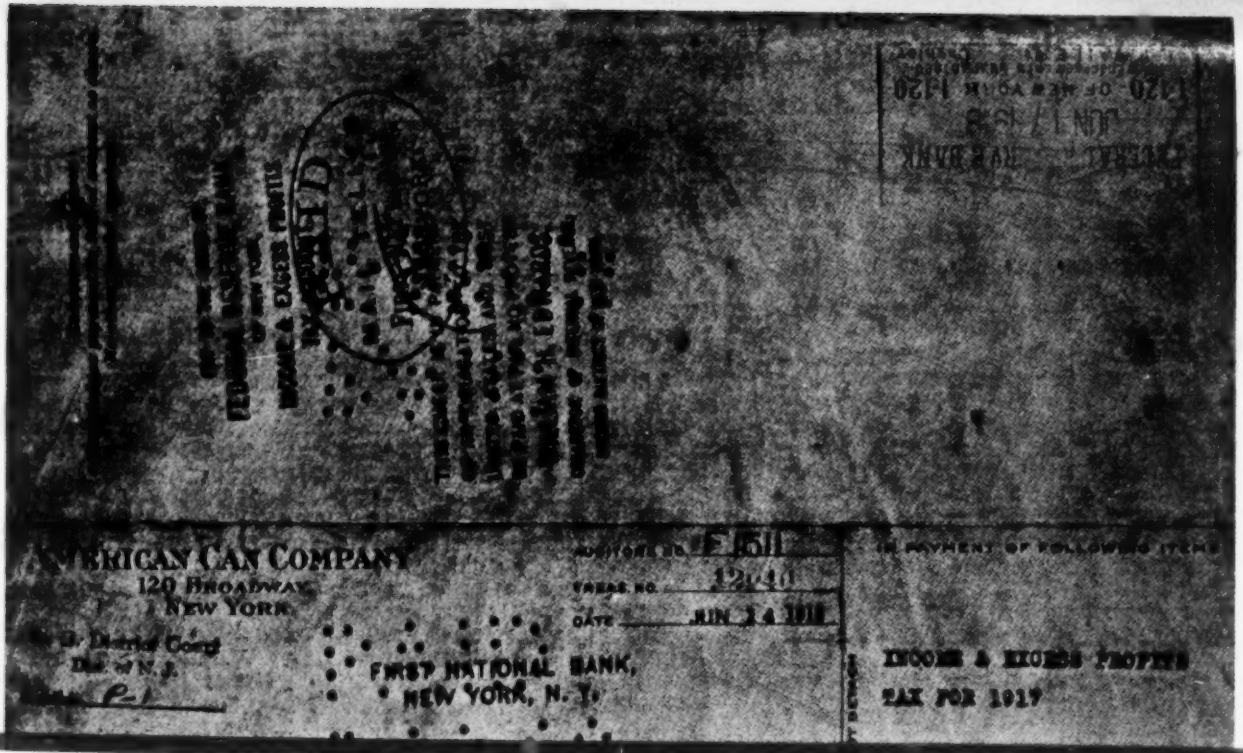
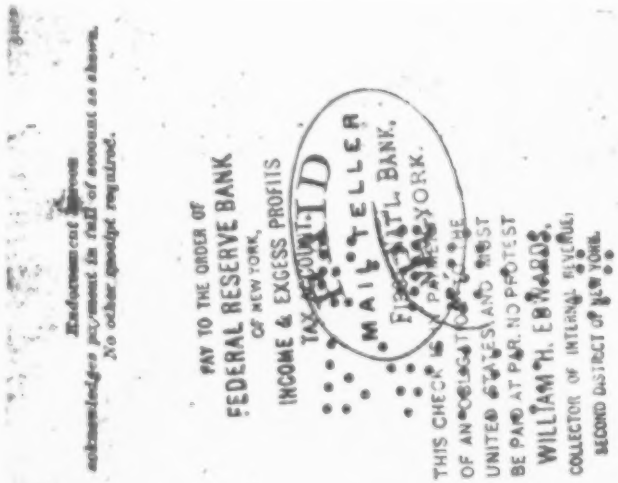

AMERICAN CAN COMPANY
120 BROADWAY
NEW YORK
P-1
AUDITOR'S NO. E 151
TREAS. NO. 12140
DATE JUN 14 1918
FIRST NATIONAL BANK,
NEW YORK, N. Y.
INCOME & EXCESS PROFITS
TAX FOR 1917

EXHIBIT P-1



AMERICAN CAN COMPANY
120 BROADWAY,
NEW YORK.

U. S. District Court
Dist. of
Exhibit P-1

AUDITOR'S NO. F1511
TREAS NO.
DATE JUN 14 1918

FIRST NATIONAL BANK,
NEW YORK, N. Y.

PAY TO WILLIAM H. EDWARDS, COLLECTOR OF INTERNAL REVENUE OR ORDER

CUSTOM HOUSE BLDG. NEW YORK.

DO NOT DETACH

IN PAYMENT OF FOLLOWING ITEMS

INCOME & EXCESS PROFITS
TAX FOR 1917

3,286,499.86

-THREE MILLION TWO HUNDRED EIGHTY SIX THOUSAND FOUR HUNDRED NINETY NINE & 86/100- -

AMERICAN CAN COMPANY.

Endorsement hereon
acknowledges payment in full of account as shown.
No other receipt required.

PAY TO THE ORDER OF
FEDERAL RESERVE BANK
OF NEW YORK,
INCOME & EXCESS PROFITS
TAX ACCOUNT

THIS CHECK IN PAYMENT
OF AN OBLIGATION TO THE
UNITED STATES NOT
BE PAID AT PAR IF

PAID
WILLIAM H. [illegible] TELLER
COLLECTOR OF INTERNAL REVENUE
SECOND DISTRICT OF NEW YORK
FIRST NATL BANK,
NEW YORK.

EXHIBIT P-2

DETROIT CAN COMPANY
120 BROADWAY,
NEW YORK.

AUDITORS NO. [illegible]
TREAS. NO. 2245
DATE JUN 1[illegible]

IN PAYMENT OF FOLLOWING ITEMS

FIRST NATIONAL BANK
NEW YORK, N.Y.

INCOME & EXCESS PROFITS
TAX FOR 1917

6287.19

PAY TO W. H. EDWARDS, COLLECTOR OF INTERNAL REVENUE OR ORDER
CUSTOM HOUSE
NEW YORK

DO NOT DETACH

- - - - - SIXTY TWO HUNDRED EIGHTY SEVEN & 19/100 - - - - DOLLARS

CORRECT [illegible]

APPROVED [illegible]

DETROIT CAN COMPANY.
[illegible]
TREASURER

GENERAL INSTRUCTIONS.

EXHIBIT P 3

102

PAY TO THE
FEDERAL RESERVE
OF NEW YORK
INCOME & EXCESS
TAX ACCOUNT

THIS CHECK IS IN
OF AN OBLIGA
UNITED STATES AND
BE PAID AT PAR
WILLIAM H.
COLLECTOR OF INT
SECOND DISTRICT

PAID
TELLER
FIRST NATL. BANK
NEW YORK

United States of America.

Treasury Department.

October 4 26.

Pursuant to [illegible] are true copies of Corporation and Corporation Excess Profits Tax Returns for 1917 (with balance sheet attached to latter return, minus statements mentioned therein), of March 28, 19 8, filed by American Can Company of New Jersey, as [illegible] on file

In witness whereof [illegible]

By [illegible]

Assistant [illegible]

1-KR-3/19/23

AUDITED

CAUTION

Read this form and all instructions carefully and fill in supplementary statement on back of return first. Totals in supplementary statement must agree with totals in face of return.

Form 1031 (Revised January, 1918.)—UNITED STATES INTERNAL REVENUE

CORPORATION INCOME TAX RETURN

(FOR ALL CORPORATIONS EXCEPT RAILROAD AND INSURANCE COMPANIES)

Return of annual net income for the calendar year 1917. / fiscal year ended Dec 31, 1917.

Name of corporation: American Can Company of New Jersey

Principal office: 120 Broadway, Borough of Manhattan, City of New York

Kind of business carried on: Manufacturers of Tinplate & Other Cans, etc. Date of organization: 1915

2752366

1. Total amount of paid-up capital stock outstanding at the close of the year. (If there is no capital stock the capital other than interest-bearing indebtedness employed in the business at the close of the year. Deficit or treasury stock must not be deducted in this item. Par only must be used and paid outstanding at the close of the year for which this return is made.)

(a) Preferred common stock: 45,000,000.00
(b) Paid-up preferred stock: 40,000,000.00
Total paid-up stock: 85,000,000.00
Capital employed in business: 31

2. Total amount of bonds or other interest-bearing indebtedness outstanding at the close of the year. (Amount of indebtedness actually secured by collateral, the subject of sale or pledge in the ordinary business of the company and exclusive also of indebtedness incurred in the purchase of securities, the income from which is not subject to tax.)

Character of obligation.	Rate of interest.	Principal.
Preferred Stock	6%	40,000,000.00
Debentures	5%	45,000,000.00
		85,000,000.00

INCOME

3. (a) Gross sales and other income from operations: 1472 [illegible]
(b) Income from rentals, interest: 22 [illegible]
(c) Income from interest (see item 2 on back of return): 34 [illegible]
(d) Income from dividends (see item 3 on back of return): 60 [illegible]
(e) Income from all other sources (see item 4 on back): 45 [illegible]
Total gross income and profits: 1640 [illegible]
Less deductions: 77 [illegible]
8. Total net income: 1562 [illegible]
Less (a) Excess profits tax (see item 12): 23 [illegible]
(b) Dividends received out of income of 1916, 1917, 1918: 23 [illegible]
Total deductions: 46 [illegible]
9. (a) Amount taxable at 2% (item 8 less total of item 8a): 1516 [illegible]
(b) Amount taxable at 1% (item 8a): 76 [illegible]
10. Amount of net income shown in item 8 derived from business transacted and capital invested in the United States: 1592 [illegible]

DEDUCTIONS

(To be corresponding Items in face of return.)

4. (a) Cost of goods sold or other property sold: 1058 [illegible]
(b) Expenses, general: 151 [illegible]
5. (a) Loss sustained (but not compensated by insurance or otherwise): 9 [illegible]
(b) Depreciation charged off: 22 [illegible]
(c) Depletion charged off: 7 [illegible]
6. (a) Interest paid except as otherwise provided in (b) and (c): 12 [illegible]
(b) Interest paid on deposits (by banks only): [illegible]
(c) Interest paid on indebtedness wholly secured by collateral: [illegible]
7. (a) Domestic taxes paid, not including income and excess profits taxes: 28 [illegible]
(b) Foreign taxes paid: 41 [illegible]
Total deductions: 77 [illegible]

TAX

11. Amount taxable at 4% (item 9c less total of item 9b): 1516 [illegible]
If a return for a fiscal year ending in 1918 is made, state number of months in such fiscal year: (Jan. 1, 1917)
Enter amount taxable by the close of the fiscal year.
12. Assessed 2% tax (2% of item 9a): 29 [illegible]
13. Amount of 1% tax (1% of item 9b): [illegible]
14. Amount of 4% tax (4% of item 11): 52 [illegible]
15. Total tax assessed: 52 [illegible]

I, the undersigned, President and treasurer of the above-named company, whose return of net income is herein set forth, being severally duly sworn, each for himself, deposes and says that the items entered in the foregoing report and in the supplementary statement and in any additional list or lists attached to or accompanying this return are, to his best knowledge and belief, true and correct in every and every particular.

Sworn to and subscribed before me this 29th day of March 1918.

SEP 1918

[illegible] Notary Public

TOTAL TAX: [illegible]
TOTAL REFUND: [illegible]
(United currency.)

[illegible] President.

[illegible] Treasurer.

104

GENERAL INSTRUCTIONS.

Excess profits tax.—For the purpose of the excess profits tax, every corporation subject to income taxation is deemed to be engaged in business, and all the trades and businesses in which it is engaged (whether continuously carried on or not) shall be treated as a single trade or business. And all its income from whatever source derived shall be deemed to be derived from such trade or business.

In the case of a trade or business having no invested capital or not more than a nominal invested capital, the excess profits tax is equivalent to 8 per cent of the net income in excess of $5,000. This tax applies primarily to corporations engaged principally in rendering personal service in which the principal income is derived from the personality and the earnings of which are to be ascribed primarily to the activities of the owners.

In the case of a trade or business having more than a nominal invested capital, the excess profits tax is equivalent to 8 per cent of the net income, depending on its ratio to the invested capital. Every corporation having a net income of over $3,000 for the taxable year must file a return of invested capital and compute the excess profits tax on Form 1031.

For further instructions see Regulations No. 41, Relative to the War Excess Profits Tax. A copy can be obtained from any collector of internal revenue.

Time of filing returns.—Returns made on the basis of a calendar year must be filed on or before March 1, with the collector of internal revenue of the district in which is located the principal place of business of the corporation; if made on the basis of a FISCAL YEAR*, they must be filed within 60 days after the close of such year.

*Fiscal year.—Corporations desiring to make returns of annual net income on the basis of a fiscal year other than the calendar year must, on or before March 1 of the year in which the return would be due if made on the calendar year basis, file with the collector a notice in writing designating the last day of the month of such fiscal year. A return for that portion of the calendar year ending with the date designated as the close of the fiscal year must be filed on or before the last day of March of the next calendar year, and the return for each full fiscal year thereafter must be filed within 60 days after the closing date of the fiscal year so designated.

Extension of time.—In the case of neglect to file the return within the prescribed time, the collector is authorized to grant a reasonable extension of time for the filing thereof, not exceeding 30 days from the normal due date, provided such neglect was due to absence or sickness and provided an application therefor is made to the collector in writing prior to the expiration of the period for which extension may be granted. In meritorious cases the Commissioner is authorized to grant such further extension of time as may be deemed proper.

Signatures and verification.—Returns must be signed and verified by two officers of the corporation, either the president, vice president, treasurer, assistant treasurer, or other principal officer, and the treasurer or other financial officer, and must be sworn to before an officer authorized to administer oaths, and the official character of each officer required to be sworn must be indicated on the return in the space provided for that purpose.

Subsidiary companies.—The corporation making this return must attach hereto a list of all its subsidiary companies, if any, with the location of the principal place of business of each. Each subsidiary company must make a separate and distinct return.

Foreign corporations.—Foreign corporations subject to the law are required to make returns to the collector of the district in which is located the principal place of business or agency through which it transacted the business in the United States, or if the corporation has no place of business or agency in the United States, its return will be filed with the collector of internal revenue at Baltimore, Maryland. The gross income to be returned is that received from business transacted and capital invested in the United States, including interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise, and including income derived from dividends on capital stock or from the profits of residents or corporations, joint-stock companies, or associations whose net income is taxable under this law. The deductions allowable are those losses and disbursements actually and necessarily incurred in the transaction of the business in this country, all as specifically set out in the Act. Foreign taxes are not deductible from the gross income arising and accruing to any foreign corporation from business done or capital invested in the United States. If a foreign corporation has no place of business or agency in the United States and no return is made, the tax on income from interest and dividends will be withheld at the source.

Penalties.—Corporations refusing or neglecting to file returns within the time prescribed by law or rendering false or fraudulent returns shall be liable to a penalty of not exceeding $10,000, and an additional tax of 50 per cent in case of neglect to file the return within the time prescribed by law, and 100 per cent in the case of a false or fraudulent return, shall be added to the assessment; provided, if in case of delinquency, if the return is voluntarily filed without action thereon from the collector, and it is shown that delay in filing same is due to reasonable cause and not to willful neglect, the 50 per cent additional tax will not be assessed. A statement of the cause of delay must be attached to each delayed return.

Any officer, agent or person required by law to make, render, sign, or verify any return, who makes any false or fraudulent return or statement with intent to defeat or evade the assessment required to be made shall be guilty of a misdemeanor, and shall be fined not exceeding $2,000 or be imprisoned not exceeding one year, or both, at the discretion of the court, with the costs of prosecution.

EXHIBIT P 4

(41)

SUPPLEMENTARY STATEMENT

The following information must be furnished, either on this sheet or on attached schedules, by every corporation, joint-stock company, or association. Without such information the return will not be accepted as complete. The items in bold relate to the correspondingly numbered items on the first page.

3. (a) FROM INTEREST.

Interest to be reported as income for the purpose of the income tax includes all interest received on bonds of municipalities exempt from interest on obligations of a State or political subdivision thereof, and upon the obligations of the United States or its possessions.

3. (d) FROM DIVIDENDS RECEIVED.

Any distribution made or ordered to be made by a corporation out of its earnings or profits accrued since March 1, 1913, whether in cash or in stock or in the form of scrip, must be returned (under Title II, (d) on front page of this form) as income of the year for which the distribution was made, and will be taxed at the rates prescribed by law for the years in which the profits were earned, viz., 1% on amounts received out of earnings or profits accrued to March 1, 1914, and 1915, and 2% on amounts received out of earnings or profits accrued in 1916 and 1917. Interest from the corporation paying the dividends is to be returned separately in this return, showing separately the amount relating to profits of each year; otherwise, they will be deemed to have been paid out of the profits of 1917 and will be taxed 2%. The receiving corporation, in order that the corporations paying dividends received in 1917 at the rates applicable to the years in which the profits were earned, must fill in the following form:

Dividends received in 1917 out of profits accrued					
1913	1914	1915	1916	1917	Total.
$	$	$	$	$	

3. (b) FROM OTHER SOURCES.

Income received from all sources not otherwise specified above must be itemized below:

4. (a) COST OF GOODS AND OTHER PROPERTY SOLD.

Report the cost of goods

4. (b) EXPENSES, GENERAL.

This item should include only the ordinary and necessary expenses paid within the year in the operation of the business and maintenance of the property, as itemized as per schedule below. It must not include any expenditures reported under 4 (a), 5, 6, or 7.

Expenditures for incidental repairs which do not add to the value or appreciably prolong the life of property are deductible as expenses, but expenditures for new buildings, permanent improvements or betterments which increase the value of property, or for restoring or replacing property, are not deductible under this or any other item of the return. Such expenditures are properly chargeable to capital account, to be extinguished through annual depreciation charges.

Payments made to officers or employees, who are stockholders, in the guise of salaries or compensation, the amount of which is based upon the stockholdings of such officers or employees, are not deductible as a business expense.

1. Salaries of officers	$
2. Salaries, wages, commissions, and other compensation of employees (not including officers or other persons properly classed under 4 (a), (b), or (c))	
3. Rents, royalties, and other payments on lease account	
4. Repairs, ordinary and incidental	
5. Other expenditures	
Total expenses	$

If salaries were increased or extra compensation paid to officers, state the amounts, the reasons for them, and the basis on which computed:

5. (a) LOSSES.

Losses deductible under this item must be sharply established in connection with sale or abandonment of property, or otherwise, and must be sustained, actually ascertained, and charged off within the year on the books of the corporation.

Kind of property sold or abandoned	Cost or other basis	
	$	
Total		

5. (b) DEPRECIATION.

The amount deductible on account of depreciation is an amount charged off which fairly represents the loss during the year in the value of physical property by reason of exhaustion, wear, and tear. Such amount should be determined upon the basis of the cost of the property and the probable number of years constituting its life. Stocks, bonds, and like securities, as well as any other intangible assets, are not subject to exhaustion, wear, and tear within the meaning of the law. Hence any amount charged off as representing a shrinkage in the value of such assets is not deductible either as depreciation or as a loss.

Depreciation computed on total average value of merchandise in stock is not an allowable deduction by reason of diminution or obsolescence the contributing to unsalability.

If a deduction is made on account of depreciation, the following statement must be filled in:

Kind of property.	Probable life after acquisition.	Amount of depreciation charged off.	
		This year.	Previous years.
		$	$

If facilities were increased during the year, state the material of which constructed.

5. (c) DEPLETION.

Depletion applies to the exhaustion of natural deposits and contemplates a deduction to return to the corporation the capital invested in the property prior to March 1, 1913, an amount sufficient to return to the corporation on this last mentioned basis or value of such deposits at the time of their exhaustion. Any [illegible] deduction must not exceed the [illegible] March 1, 1913, [illegible] to the date of the [illegible] balance with the amount sought to be [illegible] property.

[illegible] depletion charge for [illegible]

1. [illegible]
2. [illegible] March 1, 1913, if acquired by [illegible]
3. [illegible] other permanent improvements, if any
4. [illegible] depletion to date of sale
5. Net value [illegible] (item 2 plus item 3, minus item 4)

State how market value March 1, 1913, was determined

Does [illegible] deduct any [illegible] such? $

6. INTEREST PAID.

(a) The amount of interest to be allowed under (a) of the statute actually paid within the year on an existing indebtedness [illegible] on indebtedness falling under 6 (b) or 6 [illegible] for the purpose of obtaining for the purchase of obligations or securities the income from which is exempt from taxation, but not in excess of the paid-up capital stock of the [illegible] year, or if there is no capital stock, the entire amount of [illegible] indebtedness employed in the business [illegible] all of the interest-bearing indebtedness also [illegible]

Capital employed in the business, as here used, contemplates the entire capital paid in [illegible] much of the accumulated surplus as [illegible] but does not include any borrowed capital or interest-bearing [illegible]

(b) Interest paid [illegible] on loans or moneys received for investment and secured by [illegible] bonds [illegible] by a bank, banking association, or loan or trust company [illegible] so paid.

(c) If the corporation's [illegible] or any part thereof, is wholly secured by collateral which [illegible] object of the [illegible] in the corporation's ordinary business as a dealer in such property, state [illegible] paid on an amount of such indebtedness not exceeding the actual value of the collateral may be deducted.

Describe all obligations on which interest is paid in the following form. Distinguish plainly collateral loans falling under 6 (c) from [illegible] incurred for the purchase of securities, the income from which is exempt from income tax.

Kind of obligation.	Amount of principal.	Rate of interest.	Amount of interest paid.
	$		$
Total	$		$

7. (a) TAXES PAID.

Taxes paid or accrued on the books of the corporation during the taxable year, are deductible with the exception of income and excess profits taxes (including taxes paid on the interest on the bonds of the corporation in pursuance of a covenant contained therein, paid [illegible] taxes or income derived from sources within the [illegible] corporations, local taxes specially assessed against property [illegible] for public improvements or betterments, and taxes upon the operation of capital stock in the hands of the stockholders.

BASIS OF RETURN.

Is the return made on the basis of actual receipts and disbursements?

If not, describe fully what other basis or method was used in computing net income

UNDISTRIBUTED INCOME, SURPLUS, AND UNDIVIDED PROFITS.

Total net income of taxable year preceding that for which this [illegible] (as shown in item 9 thereof)	$
Amount [illegible] remaining undistributed six months after [illegible]	
Amount [illegible] remaining undistributed twelve months after [illegible]	
Total undistributed profits of preceding taxable year	

If sufficient space [illegible] for any of the information required in the "Supplementary Statement," [illegible] the item indicated, marked with the number [illegible] attached to this form.

EXHIBIT P 4

CAUTION.
Read all instructions.
Answer all questions.
If necessary, ask your Collector or Internal Revenue for assistance.

CORPORATION EXCESS PROFITS TAX RETURN

(Do not write in this space.) RECEIVED

Taxable year ended December 31st, 1917.

Name: American Can Company

Business address: 120 Broadway, South Fork City

Kind of business: Manufacturers of Tin Cans, Sheet Metal and Tobacco Containers. Date established: March 9th, 1901.

GENERAL INSTRUCTIONS.

(39)

2752366

1. **Complete instructions.**—For complete instructions concerning the filling of this form see Regulations No. 41 relative to the War Excess Profits Taxes imposed by the War Revenue Act approved October 3, 1917, referred to hereinafter as Excess Profits Tax Regulations. Copies can be obtained from any collector of internal revenue.

2. **Who must make a return on Form 1103.**—Every corporation having for the taxable year a net income of $1,000 or more (see Form 1031) must make a return on this form of its average invested capital during the taxable year and compute the amount of its excess profits tax, if any, as directed herein.

This return should be made at the same time and in the same manner as the return of net income for the taxable year on Form 1031.

A corporation which claims that it employs in its business only a nominal capital or that it can not satisfactorily determine the amount of its invested capital must, nevertheless, fill this form so far as practicable in order to show the facts necessary for action on its claim.

3. **Taxable year.**—The taxable year is the calendar year 1917 or (if the fiscal year of the corporation differs from the calendar year) the fiscal year ending in the calendar year 1917. A corporation whose fiscal year differs from the calendar year may also use this form for its return (without entries for prewar period) covering the fiscal year ending in 1918.

4. **Taxable income.**—All the income of a corporation from whatever source derived is deemed to be derived from its business and all such income subject to the income tax is also subject to the excess profits tax except as provided for in Schedule I.

5. **Deduction.**—Each corporation whose income (derived from a business carried on with invested capital) is subject to excess profits tax may deduct from the amount of its taxable income (1) an amount equal to not less than 7 per cent and not more than 9 per cent of the amount of its invested capital as explained below, and (2) $3,000.

If the corporation was not in existence during the whole of at least one of the calendar years 1911, 1912, and 1913, designated by the act of October 3, 1917, as the prewar period, and has not succeeded to the control of a business which was carried on during any one or more of those years, the first deduction is an amount equal to 8 per cent of the amount of invested capital. Otherwise the deduction is an amount equal to the same percentage of the invested capital for the taxable year as the average net income during the prewar period was of the average invested capital during that period, provided that if such percentage is less than 7 per cent, the deduction shall be computed at the rate of 7 per cent and if more than 9, at the rate of 9 per cent (see Excess Profits Tax Regulations Article 21).

In order to take advantage of this provision the corporation must make a return of invested capital during the prewar period as well as during the taxable year. Space for such a return is provided on this form.

If the corporation prefers, it may compute the deduction at the rate of 7 per cent and avoid the necessity of rendering a return of invested capital for the prewar period. In any case the average amount of invested capital during the taxable year must be determined if possible.

6. **Invested capital.**—For definition of "invested capital" and complete instructions for computing its amount see Excess Profits Tax Regulations, Articles 42 to 63.

7. **Computation of tax for fiscal year, part of which falls in the calendar year 1917.**—The tax of a corporation whose fiscal year differs from the calendar year shall be that proportion of the tax computed on the net income for the fiscal year which the number of months from January 1, 1917, to the end of the fiscal year bears to the entire number of months in the fiscal year.

8. **Corporations making claim for assessment under Article 82 of the Regulations** (section 210 of the act of October 3, 1917) should answer all questions and fill all schedules so far as possible and attach a statement explaining why it is impracticable or, in the case of foreign corporations, unreasonably expensive to fill out the entire return.

SCHEDULE I.—NET INCOME FOR TAXABLE YEAR SUBJECT TO EXCESS PROFITS TAX.

Net income for taxable year shown in Item 8, Form 1031	$ 17994406 46
Plus interest on obligations of the United States issued since September 24, 1917, held by corporation in excess of $5,000 par value	
TOTAL	17994406 46
Less (a) Dividends received, as shown in Item 8d, Form 1031	$ 600 00
(b) Interest paid (not in excess of legal limit) on indebtedness incurred for purchase of obligations specified in Item 7 above	
NET INCOME SUBJECT TO EXCESS PROFITS TAX	$ 17993806 46

SCHEDULE II.—INVESTED CAPITAL.

ITEM.	1913	1914	1915	TAXABLE YEAR.
1. Capital, surplus, and undivided profits at the close of the preceding year as shown by corporation's books before making any adjustments therein (from Schedule A)	$	$	$	$ 96111651 70
2. Adjustments by way of additions (from Schedule B)				1559 50
3. TOTAL				97113211 20
4. Adjustments by way of deductions (from Schedule C)				1192766 11
5. Invested capital at beginning of year (Item 3 less Item 4)				97113211 20
6. Changes in invested capital during year (from Schedules D and E)				1192766 11
7. Invested capital for year				97019277 66
8. TOTAL INVESTED CAPITAL FOR PREWAR PERIOD				

SCHEDULE III.—DEDUCTION.

1. Percentage—net income to invested capital for prewar period. (Item 4, Schedule F, divided by Item 4, Schedule II.) Carry out results as far as desired, but drop the remainder, if any, without increasing the last figure of the percentage	%
2. Percentage to be used in computing deduction (see Instruction 5)	7 %
3. Amount of deduction computed at above rate on invested capital for taxable year	$ 6791926 44
4. Exemption (except for foreign corporations)	$ 3000 00
TOTAL DEDUCTION	$ 6794926 44

SCHEDULE IV.—COMPUTATION OF TAX.

CLASSES OF INCOME FOR COMPUTATION OF TAX. Over—	But not over—	Amount of income in each class	Deduction (if in excess of 15 per cent of invested capital, enter only 15 per cent on first line and leave on line of next class)	Balance subject to tax	Rate	AMOUNT OF TAX.
1	2	3	4	5	6	7
$0.00	15 % of invested capital	$ 11655190664	6794926644	4860263420	20%	$ 1535710284
15 % of invested capital	20 % of invested capital	3381413322		3381413322	25%	1186703330
20 % of invested capital	25 % of invested capital				35%	
25 % of invested capital	33⅓ % of invested capital				45%	
33⅓ % of invested capital					60%	
TOTAL		$ 15036603986	6794926644	8241676742		$ 2721414114

a3

EXHIBIT P 4

SCHEDULE A.—CAPITAL, SURPLUS, AND UNDIVIDED PROFITS AS SHOWN BY BOOKS BEFORE MAKING ANY ADJUSTMENTS THEREIN.

ITEM	1917	1913	1914	TAXABLE YEAR
Capital stock (or trust fund) outstanding at the close of the year (not including treasury stock):				
1. Preferred				
2. Second preferred				
3. Common				
4. Total				
Part or all contributed surplus:				
5. Paid-in surplus				
6. Earned surplus				
7. Undivided profits				
8. Grand total of items 4, 5, 6, and 7				

SCHEDULE B.—ADJUSTMENTS BY WAY OF ADDITIONS.

B1. If any part of the interest on the corporation's permanent indebtedness was excluded in computing its invested capital for the taxable year (see Form 1031, a proportionate part of such indebtedness may be added to invested capital for that year as Item 1, Schedule B.

B2. If any addition to invested capital is reported in Item 2, Schedule B, submit a full statement showing the kind of property, the date when paid in, its value on that date, and how its value was determined.

B3. If any addition to invested capital is reported in Item 3, Schedule B, submit a statement showing the kind of property, the date when acquired, the cost to the present owner, and the cost to the transferor if acquired by gift, bequest, devise, or inheritance.

B4. If any addition to invested capital is reported in Item 4, Schedule B, state specifically the amount of depreciation or depletion sustained each year in the books of the company and the amount allowed as a deduction in computing taxable income.

ITEM	1911	1912	1913	TAXABLE YEAR
1. Total amount of permanent indebtedness, the interest on which is not deductible in computing income tax (Article 6)				
2. Value of taxable property in excess of par value of stock issued therefor				
3. Adjustment (as per account allowable under Article 6)				
4. Deduction claimed on account of corporations [illegible] by Treasury Department as per [illegible]				
5. [illegible]				
6. [illegible]				
7. [illegible]				
8. Total				

SCHEDULE C.—ADJUSTMENTS BY WAY OF DEDUCTIONS.

C1. Is any good will, trade-mark, trade brand, franchise, or similar intangible property, such as for stock entered on the books of the corporation at a value in excess of its [illegible] when paid in? _____ In excess of the par value of the stock issued therefor? _____

If so, submit a statement showing (a) date of acquisition; (b) cash value at that date; (c) par value of stock issued therefor; (d) par value of total stock outstanding on March 1, 1913; and (e) value at which the same are entered on the books of the corporation.

The amount by which "a" exceeds "b," "c," or 20 per cent of "d," whichever is lowest, must be entered as Item 1, Schedule C, for the taxable year and for each year of the present period that is affected.

C2. Is any patent or copyright paid in for stock entered on the books of the corporation at a value in excess of its actual cash value when paid in? _____ In excess of the par value of the stock issued therefor? _____

If so, submit a statement showing (a) date of acquisition; (b) cash value at that date; (c) par value of the stock issued therefor; and (d) value at which the patent or copyright is entered on the books of the corporation.

The amount by which "a" exceeds "b" or "c," whichever is the lower, must be entered as Item 2, Schedule C, for the taxable year and for each year of the present period that is affected.

C3. Is any tangible property, paid in for stock entered on the books of the corporation at a value in excess of its actual cash value when received? _____ In excess of the par value of the stock paid therefor? _____

If any tangible property paid for specifically with stock before January 1, 1914, entered on the books of the corporation at a value in excess of its actual cash value on that date:

If the answer to any of the foregoing questions is "yes," submit a statement showing (a) kind of property; (b) when acquired; (c) par value of the stock paid therefor; (d) actual cash value of the property when paid in; (e) actual cash value of the property on January 1, 1913, if paid in before that date; (f) basis of the valuation stated under "e"; (g) value at which the property is entered on the corporation's books; and (h) amount by which each value exceeds the allowable value under Article 6b of the Excess Profits Tax Regulations. Enter the amount as Item 3, Schedule C, for the taxable year and for each year of the present period that is affected. (Note that the value January 1, 1913, does not affect the present period.)

C4. (a) Was any stock issued by the corporation received as gift or for a consideration substantially less than its par value? No (b) If so, what was the par value of such stock? _____ (c) What amount of cash or its equivalent was derived from the issue of such stock? $ _____

The excess of "b" over "c" must be entered as Item 4, Schedule C, for the taxable year and for each year of the present period that is affected.

C5. Was the business organized or established, or was its ownership changed after March 1, 1913? No If so, answer the following questions:

(a) Did an interest in the business of 50 per cent or more remain in the control of the same persons, corporations, combinations or partnerships, or of any of them? _____

(b) Were any of the assets entered on the books of the corporation making this return at a higher value than on the books of its predecessor? _____

(c) If so, were such assets paid for specifically as such in cash or tangible property? _____

The increase in book value of any property for which paid for must be deducted from the invested capital for the taxable year as Item 5, Schedule C, unless it can be shown that under the excess profits law and regulations the property was undervalued on the books of the predecessor business.

C6. Is any property paid for with cash or with other tangible property entered on the books of the corporation at a value in excess of the amount of cash paid therefor or the actual cash value of the tangible property paid therefor? No If so, submit a statement showing (a) kind of property; (b) amount of cash paid therefor; (c) actual cash value of other tangible property paid therefor; (d) how that value was determined; (e) value at which the property is entered on the books of the corporation; and (f) excess of "e" over "b" or "c." This excess must be entered as Item 6, Schedule C, for the taxable year and for each year of the present period that is affected.

C7. Has adequate provision been made in the expense accounts of the company for (a) losses of every kind? Yes (b) depreciation? Yes (c) obsolescence? Yes (d) depletion of mineral deposits, timber supplies and the like? [illegible] (e) [illegible]

If adequate charge has not been made for depreciation, depletion, obsolescence, and other losses, and the value of the property has not been maintained by replacements that have been charged to expense, proper additional charges for depreciation must be computed for all years in which they were not made on the books, and the total amount of such charges must be entered as Item 7, Schedule C, for the taxable year (and for each year of the present period that was affected) and deducted in arriving at its surplus and undivided profits.

C8. Has the corporation any stocks, bonds (other than obligations of the United States), or other assets, the income from which is not subject to excess profits tax? Yes If so, at what value are they carried on the corporation's books? $ 1,000,000.00 Has any portion of such assets been included in invested capital in accordance with Article 45 and 46 of the Excess Profits Tax Regulations? No If so, how much? $ None Is the balance in excess of the corporation's indebtedness, excluding the amount thereof that has been included in invested capital as Item 1, Schedule B? No If so, state the amount of such excess. $ None

Enter this amount as Item 8 in Schedule C, for the taxable year, and make a similar correction for each year of the present period.

EXHIBIT P-4

a4

SCHEDULE C.—ADJUSTMENTS BY WAY OF DEDUCTIONS (Continued)

ADJUSTMENT ON ACCOUNT OF—	1917	1918	1919
1. Value (if any) of good will, trade-marks, trade brands, franchises, or other intangible property purchased with stock (Articles 57 and 58)			
2. Valuation of patents and copyrights paid in for stock (Article 59)			
3. Valuation of tangible property paid in for stock (Article 58)			
4. Stock returned to corporation as a gift, etc. (Article 54)			
5. Valuation of assets acquired in reorganization (Article 50)			
6. Appreciation (Article 48)			
7. Depreciation and depletion (Article 47)			
8. Excess of stocks and other taxable assets over indebtedness (Article 44)			
9.			
10.			
11. Total deductions			

SCHEDULE D.—CHANGES IN INVESTED CAPITAL DURING TAXABLE YEAR.

Specify (by using red ink for distributions, or otherwise) whether each item represents an addition or a distribution.

Report dividends paid out of profits of prior years but not dividends paid out of profits of the taxable year.

In column 4 enter the number of whole months remaining in the year, plus a fraction consisting of the number of days remaining in the month (including the date of change) divided by the total number of days in the month.

Assets (other than cash) paid in for stock, must be valued in accordance with Articles 56 to 60 of the Excess Profits Tax Regulations.

Nature of additions and distributions	Date	Amount	Number of months (fractions)	Adjusted average (Column 3 × column 4)
1. Dividend Paid (Distribution)	January 25, 1917	75	12	75
2.				
3.				
4.				
5.				
6.				
7.				
8.				
9.				
10.				
11.				
12.				
13.				
14.				
15.				
16.				
17.				
18. Net addition or reduction				75

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SCHEDULE E.—CHANGES IN INVESTED CAPITAL DURING PREWAR PERIOD.

See instructions under Schedule D. Compute net addition or reduction *separately* for each year.

Nature of additions and distributions	Date	Amount	No. of months	Adjusted average (Column 3 × column 4)
1.				
2.				
3.				
4.				
5.				
6.				
7.				
8.				
9.				
10.				
11.				
12.				
13.				
14.				
15.				
16.				
17.				
18.				

SCHEDULE F.—NET INCOME DURING PREWAR PERIOD.

ITEM.	1911	1912	1913
1. Net income for year as reported on income tax return. (Do not include figures for less than a whole year's income)			
2. Plus amount of Federal income tax paid during year			
3. Total for each year			
4. Less amount of dividends credited to 1913			
5. Net totals for year 1913			
6. Grand total for PREWAR period			

65

EXHIBIT P 4

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QUESTIONS.

4. Explain the nature of the corporation's business:
   (a) Main business
   (b) Collateral businesses, if any

2. Date of incorporation [illegible] Under the laws of what State or country? New Jersey

4. Enter on the following lines the names and addresses of three principal concerns in your locality engaged in the same kind of business

5. What was the fair value of the total capital stock of the corporation as determined in the last assessment of the capital stock tax (if any)? Specify the year

6. If any patent is included among your assets, attach a schedule to this return showing for each patent its serial number, date of issue, name of patentee, amount of cash or stock paid

7. If the corporation ever took over a going business or otherwise acquired a mixed aggregate of tangible property, patents, and copyrights, and good will and other similar intangible property, and paid for such property in whole or in part with stock or other securities, submit a statement showing—
   (a) The name of the concern taken over (or from which the property was acquired)
   (b) The nature of the assets and liabilities so acquired
   (c) The total par value of the stock issued therefor
   (d) The value at which each class of assets was carried on the books of the concern from which acquired. If obtainable submit a balance sheet of the predecessor corporation as at the date of acquisition.
   (e) The value at which each item was entered on the books of the corporation making this return. The different classes of property must be valued as prescribed by Article 59 of the Excess Profits Tax Regulations and the values so obtained must be used in making adjustments in I, J, and K, Schedule C.

   If patents or copyrights were acquired, state the basis on which their value was determined, and how they were paid for.

   If good will or other intangible assets were acquired, state the basis on which their value was determined, and how they were paid for.

8. Is the corporation affiliated with one or more other corporations within the meaning of Article 77 of the Excess Profits Tax Regulations? If so, submit a statement describing all its intercorporate relationships.

9. Is this return a consolidated return which the affiliated corporations are entitled to make under Article 77 of the Excess Profits Tax Regulations? If so, submit a schedule showing in detail the computation of the consolidated

10. If the corporation was not in existence during the whole of the years 1911-1913, is its business substantially a continuation of a business carried on during any part of those years? If so, give name and address of the concern by which, and address at which, its business was then carried on

11. Submit

   (a) The balance sheet of the corporation as

   (b) The balance sheet of the corporation as

We, the undersigned, president and treasurer of the corporation, being severally duly sworn, each for himself deposes and says that the foregoing return, including the accompanying schedules and statements, has been examined by him and is to the best of his knowledge and belief a true and complete return made in accordance with the Excess Profits Tax Regulations.

Sworn to and subscribed before me this 29 day of

President.

Treasurer.

EXHIBIT P 4

Sept 18
15

f.1-339

United States of America.

Treasury Department,

October 8 1926.

Pursuant to Section 882 of the Revised Statutes I hereby certify that the annexed are true copies of Corporation and Corporation Excess Profits Tax Returns for 1917 (with balance attached to latter return), executed March 29, 1918, filed by Can Company (of New Jersey), New York City, on file

Department

In witness whereof, I have hereunto set my hand and caused the seal of the Treasury Department to be affixed on the day and year first above written.

By direction of the Secretary of the Treasury:

Assistant Secretary of the Treasury.

CAUTION

Read this form and all instructions carefully and fill in supplementary statement on back of return here. Totals in supplementary statement must agree with totals on face of return.

Form 1031 (Revised January, 1918) UNITED STATES INTERNAL REVENUE

CORPORATION INCOME TAX RETURN

(FOR ALL CORPORATIONS EXCEPT RAILROAD AND INSURANCE COMPANIES)

Return of annual net income for the { calendar year 1917 / fiscal year ended Dec 31st 1917

Name of corporation [illegible] Company of New Jersey

Principal office [illegible] Broadway [illegible] City [illegible]

Kind of business carried on Manufacturers of Coal Tar Products and Crude Drugs Date of organization May 17th 1902

Internal Revenue Use Only: Date Received [illegible] 1918; 2752835

1. Total amount of paid-up capital stock outstanding at the close of the year, or if there is no capital stock the capital other than interest-bearing indebtedness employed in the business at the close of the year. Unissued or treasury stock must not be included in the item, but only stock actually issued and outstanding at the close of the year for which this return is made.

(a) Paid-up "common stock" $ 1,500,000.00

(b) Paid-up "preferred stock" $ 1,000,000.00

Total paid-up stock $ 2,500,000.00

or (c) Capital employed in business $

2. Total amount of bonded or other interest-bearing indebtedness outstanding at the close of the year, exclusive of indebtedness wholly secured by collateral the subject of sale or hypothecation in the ordinary business of the company and exclusive also of indebtedness incurred in the purchase of securities, the income from which is not subject to income tax.

Class (kind of indebtedness)	Rate of interest	Principal
[illegible]	6%	$ [illegible]
[illegible]	[illegible]	$ [illegible]
Total indebtedness		$ [illegible]

INCOME

3. (a) Gross sales and other income from operations	8	6223,161.99
(b) Income from rentals, royalties, etc.		141.72
(c) Income from interest (add item 2c on back of return)		44,09.93
(d) Income from dividends (add item 3d on back of return)		[illegible]
(e) Income from all other sources (see item 3e on back)		[illegible]
Total gross sales and other income		[illegible]
Less total deductions		5521,766.56
4. Total net income		1044,766.64
Less net income profits tax (item 12)		[illegible]
Net income subject to normal tax (item 7 less item 11)		[illegible]
Dual (6 plus 6)		[illegible]
5. Amount (1% per cent) (multiply item 4 or item 7 by 1½ per cent)		[illegible]
6. (a) Amount (2% per cent) (multiply item 4 or item 7 by 2 per cent)		1044,766.64
(b) Dividends received (item 3d) $		
Total (a plus b)		
7. Amount (item 4 or item 7 less total of 6 plus b)		1044,766.64

If return is made for a full fiscal year ended in 1917, compute tax on net income for twelve months from January 1, 1917, to the close of the fiscal year. Enter amount here.

DEDUCTIONS

(See corresponding items on back of return)

4. (a) Cost of goods sold or other property sold	5521,766.56
(b) Expenses, general [illegible]	1652,774.91
5. (a) Losses sustained [illegible]	[illegible]
(b) Depreciation charged off [illegible]	1652,22
(c) Depletion charged off	[illegible]
6. (a) Interest paid (from 2c and 3d, items 2b and c)	[illegible]
(b) Interest paid on deposits (for banks only)	[illegible]
(c) Interest paid on indebtedness wholly secured by collateral	[illegible]
7. (a) Domestic taxes paid, not including income and excess profits taxes	6749.45
(b) Foreign taxes paid	[illegible]
	5521,766.56

TAX

12. Amount of excess profits tax (see instructions below)	
13. Amount of 2% tax (2% of item 9a)	2089.53
14. Amount of 1% tax (1% of item 9b)	
15. Amount of 4% tax (4% of item 11)	41,911.41
16. Total tax assessable	41,911.41

We, the undersigned, president and treasurer of the above-named company, whose return of net income is herein set forth, being severally duly sworn each for himself, deposes and says that the items entered in the foregoing report and in the supplementary statement and in any additional list or lists attached to or accompanying this return are, to his best knowledge and belief, true and correct in each and every particular.

Sworn to and subscribed before me this 29 day of March, 1918

Seal of officer taking affidavit

[illegible] Notary Public

(Official capacity.)

[illegible] President

[illegible] Treasurer.

GENERAL INSTRUCTIONS.

Excess profits tax.—For the purpose of war excess profits tax every corporation subject to income tax shall be deemed to be engaged in business, and all the trades and businesses in which it is engaged (or which is customarily carried on or not) shall be treated as a single trade or business, and all its income from whatever source derived shall be deemed to be received in such trade or business.

In the case of a corporation having no invested capital or not more than a nominal capital, the excess profits tax is equivalent to 8 per cent of the net income in excess of $3,000. This applies especially to a partnership engaged principally in rendering personal services in which the employment of capital is not necessary and the earnings of which are to be ascribed principally to the activities of the members.

If the corporation has or uses more than a nominal invested capital, the excess profits tax is equivalent to eight per cent of the net income, depending on its ratio to the invested capital, as provided in section 201 of the law. Every year the taxpayer makes a return of invested capital and computes the amount of tax on Form 1009.

For further information see Regulations No. 41, Relative to the War Excess Profits Tax. A copy can be obtained from any collector of internal revenue.

Time of filing returns.—Returns covering the basis of a calendar year must be filed on or before March 1 with the collector of internal revenue of the district in which is located the principal place of business of the corporation, if it has one in the United States. If not, the return must be filed within sixty days after the close of each fiscal year.

Fiscal years.—Corporations desiring to make returns of annual net income upon the basis of a fiscal year other than the calendar year must, not later than 60 days prior to March 1 of the year in which the fiscal year begins, file with the collector of the district in which is located the principal place of business of such corporation, or if it has no place of business in the United States, then with the collector at Baltimore, Maryland, a written application stating the last day of some month as the close of each fiscal year. A return for that period of twelve months ending with the date designated as the close of the fiscal year must be filed on or before the last day of March of the next calendar year, and the return for each fiscal year thereafter must be filed within sixty days after the close of the fiscal year so established.

Extension of time.—In the case of inability to file the return within the prescribed time, the collector is authorized to grant an extension of the filing period not exceeding 30 days from the normal time fixed by law, provided such corporation shall have applied for such extension in writing prior to the expiration of the period for which extension may be granted. In such circumstances the Commissioner is authorized to grant such further extension as he may deem proper.

Signatures and verification.—Returns must be signed and verified by two officers of the corporation, that is, by the president, vice president, or other principal officer, and the treasurer or other financial officer, and must be sworn to before an officer authorized to administer oaths, and the seal of the attesting officer, if he is required to have a seal, must be impressed on the returns in the space provided for that purpose.

Subsidiary companies.—The corporation making this return must attach hereto a list of all its subsidiary companies, if any, with the location of the principal place of business of each. Each subsidiary company must make a separate and distinct return.

Foreign corporations.—Foreign corporations subject to the law are required to make returns to the collector of the district in which is located the principal place of business or agency through which is transacted the business in the United States, or if the corporation has no place of business or agency in the United States, its return will be filed with the collector of internal revenue at Baltimore, Maryland. The gross income to be returned is that received from business transacted and capital invested in the United States, including interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise, and including income derived from dividends on capital stock or from net earnings of resident corporations, joint-stock companies, or associations which are not income in taxable under this law. The deductions allowable are those losses and disbursements incident and necessary to the prosecution of the business in the country, all as specifically set out in the Act. Foreign taxes are not deductible from the gross income arising and accruing to a foreign corporation from business done or capital invested in the United States. If a foreign corporation has no place of business or agency in the United States and no return is made, the tax on income from interest and dividends will be withheld at the source.

Penalties.—Corporations refusing or neglecting to file returns within the time prescribed by law or rendering false or fraudulent returns shall be liable to a penalty of not exceeding $20,000, and an additional tax of 50 per cent in case of neglect to file the return within the time prescribed by law, and 100 per cent in the case of a false or fraudulent return, shall be assessed and collected in the manner provided, in case of delinquency, if the return is voluntarily filed without notice from the collector, and it is shown that delay in filing was due to reasonable cause and not to willful neglect, the 50 per cent additional tax will not be assessed. A statement of the reasons for delay must be attached to each delayed return.

Any officer of any corporation required by law to make, render, sign, or verify any return who makes any false or fraudulent return or statement with intent to defeat or evade the assessment required to be made shall be guilty of a misdemeanor, and shall be fined not exceeding $2,000 or be imprisoned not exceeding one year, or both, at the discretion of the court, with the costs of prosecution.

EXHIBIT P 5

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SUPPLEMENTARY STATEMENT

The following information must be furnished, either on this sheet or on an attached sheet, by every corporation, joint-stock company, or association. Without such information the return will not be accepted as complete. The items must be answered in the exact manner indicated by numbers and letters.

3. (c) FROM INTERESTS.

Interest to be reported as income for the purpose of the income tax includes all interest received on bonds or securities issued by the corporation, except interest on obligations of a State or political subdivision thereof or interest upon the obligations of the United States or its possessions.

3. (d) FROM DIVIDENDS RECEIVED.

Any distribution made or ordered to be made by a corporation out of its earnings or profits accrued since March 1, 1913, which is not entirely out of the paying company, must be returned (under Item 3 (d) of front page of this form) by the receiving corporation as income of the year in which such distribution was made or ordered to be made and will be taxed at the rates prescribed by law for the years in which such earnings or profits distributed were earned, viz, 1% on dividends received out of earnings of 1913 (reduction to March 1, 1913), 1914, and 1915, and 2% on amounts received from earnings of 1916 and 1917. A statement from the corporation paying the dividends included herein should be attached to this return, showing separately the amount of dividends paid out of earnings of each year; otherwise, they will be deemed to have been paid out of the earnings of 1917 and will be taxed 2%. The receiving corporation in order that tax may be computed on dividends received in 1917 at the rates applicable to the years in which the profits were earned, must fill in the following form:

Dividends received in 1917 out of profits earned each year subsequent to March 1, 1913.

1913	1914	1915	1916	1917	Total.
$	$	$	$	$	$

3. (e) FROM OTHER SOURCES.

Income received from all sources not elsewhere specified should be itemized below:

See P & L front page	$		
Total	$		

4. (a) COST OF GOODS AND OTHER PROPERTY SOLD.

Report the cost of goods sold in the following form:

Merchandise bought for sale	$		
Cost of manufacturing or otherwise producing goods sold (if separately shown on books). (Submit schedule showing principal items of cost).			
Plus inventories at beginning of year			
Total	$		
Less inventories at end of year			
Net cost of goods sold	$		

Explanations

If the corporation makes inventories of merchandise or material, explain the basis on which they are made, whether (a) at cost, or (b) at cost or market value, whichever is lower. If no inventories are made, make no entries referring to inventories, but report the total cost of goods purchased or produced during the year. If the cost of manufacturing or otherwise producing goods is not kept separate from general expenses in the corporation's accounts, include such cost in "Expenses, general," below.

Corporations dealing in real estate, and any corporation that has sold any of its capital assets during the taxable year, should report the cost of the property sold in the following form:

1. Original cost of property ..... $
2. Market value March 1, 1913, if acquired before that date .....
3. Cost of sales (agent, improvements, if any .....
4. Depreciation and depletion to date of sale .....
5. Net cost (item 1 or item 2 plus item 3 minus item 4) .....

State how market value March 1, 1913, was determined .....

Does such value include any good will? If so, how much? $.....

4. (b) EXPENSES, GENERAL.

This item should include only the ordinary and necessary expenses paid within the year in the operation of the business and maintenance of the properties of the corporation, itemized as per schedule below. It must not include any expenditures reported under 4 (a), 5, 6, or 7.

Expenditures for incidental repairs which do not add to the value or appreciably prolong the life of property are deductible as expended, but expenditures for new buildings, permanent improvements or betterments which increase the value of property or for restoring or replacing property, are not deductions under this or any other item of the return. Such expenditures are properly chargeable to capital account, to be extinguished through annual depreciation charges.

Payments made to officers or employees, who are stockholders, in the guise of salaries or compensation, the amount of which is based upon the stockholdings of such officers or employees, are not deductible as a business expense.

1. Salaries of officers	$	See P & L front page
2. Salary, wages, commissions, etc., (not included in "Cost of manufacturing or otherwise producing goods" under 4 (a))		
3. Rents, royalties, and other payments in lieu of rent		
4. Repairs, ordinary and incidental		
5. Other expenditures (classify)		
Total expenses	$	

If salaries were increased or extra compensation was paid to officers, state the amounts, and the basis on which computed .....

5. (a) LOSSES.

Losses deductible under this item must be distinguished from depreciation, which includes ordinary exhaustion, wear, and tear. The losses must be actually sustained during the year, must be absolute, complete, actually sustained during the year, and charged off on the books of the corporation.

Kind of property on which loss is claimed.	Cost of property.	Cause of loss.	Amount charged off within year.
	$		$
Total			

When were the deducted losses ascertained to be such? .....

How were they ascertained? .....

The cost of property lost should be determined as indicated in item 4 (a).

A bad debt, originating (income accrued since January 1, 1909, will not be allowed as a deduction unless the amount was reported as income for the year in which the debt was created.

State how the debts charged off (if any) were ascertained to be worthless .....

If at any future time a debt charged off as worthless is collected the amount collected must be returned as income for the year in which received.

Unpaid liabilities are not deductible in made good by recovery of property sold or retention of property pledged.

3 11 c

5. (b) DEPRECIATION.

The amount deductible on account of depreciation is an amount *charged off* which fairly measures the loss during the year in the value of physical property by reason of exhaustion, wear, and tear. Such amount should be determined upon the basis of the cost of the property and the probable number of years constituting its life. Stocks, bonds, and like securities, as well as any other intangible assets, are not subject to exhaustion, wear, and tear within the meaning of the law. Hence any amount entered for or representing a *shrinkage* in the value of such assets is not deductible either as depreciation or as a loss.

Depreciation computed on total invoice value of merchandise in stock is not an allowable deduction by reason of damage or obsolescence the particular is not deductible.

If a deduction is made on account of depreciation, the following statement must be filled in:

Kind of property.	Its cost.	Probable life after acquisition.	Amount of depreciation charged off. This year.	Previous years.
Buildings	$	7 1/2 yrs	$ 5,644.00	$ 25,244.95
Office Furniture		Over 10 yrs		
Office Equipment		5 yrs	11,353.21	11,188.07
Total	$		$ 16,997.21	$ 36,433.02

If built-ins, state under "Kind of property" the material of which constructed.

5. (c) DEPLETION.

Depletion applies to the exhaustion of natural deposits, and contemplates a deduction to return to the corporation the capital invested, or in case of purchase prior to March 1, 1913, an amount sufficient to return to the corporation the fair market price or value of such deposits as of that date. An allowable deduction on account of depletion must not exceed the fair market value as of March 1, 1913, or the cost subsequent to that date, of the product mined and sold during the year, and will be determined in accordance with the rule set out in Articles 170 to 172, Regulations 33, Revised. The amount sought to be deducted on this account must be charged off on the books of the company.

Kind of property.	Interest acquired (or discovered) subsequent to March 1, 1913.	Fair market value as of March 1, 1913.	Amount of depletion charged off. This year.	Previous years.
	$	$	$	$
				Amt.

If acquired subsequent to March 1, 1913, state how cost was determined .....

If acquired prior to March 1, 1913, state how fair market value as of March 1, 1913, was determined .....

6. INTEREST PAID.

(a) The amount of interest deductible under (c) in the amount actually paid within the taxable year on account of bonds, notes, or other indebtedness (except on indebtedness falling under (b) or (c) of Section 9) of indebtedness incurred for the purchase of obligations or securities (or the income from which is exempt from income tax) not in excess of the paid-up capital stock outstanding at the close of the year, or if there is no capital stock, the entire amount of capital (not including interest-bearing indebtedness) employed in the business at the close of the year, plus, in each case, one-half of the interest-bearing indebtedness also then outstanding.

Capital employed in the business, as here used, contemplates the entire capital paid in by the stockholders of the company, including in such case accumulated surplus as is actually employed in the business, but does not include any borrowed capital or interest-bearing indebtedness.

(b) Interest paid (by banks) on deposits or on money received for investment and secured by interest-bearing certificates of indebtedness issued by a bank, banking association, or loan or trust company is deductible in the entire amount so paid.

(c) If the corporation's indebtedness, or any part thereof, is wholly secured by collateral which is the subject of sale or hypothecation in the corporation's ordinary business as a dealer in such property, the interest paid on an amount of such indebtedness not exceeding the actual value of the collateral may be deducted.

Describe all obligations on which interest is paid in the following form. Distinguish plainly collateral loans falling under 6 (c) and also obligations incurred for the purchase of securities, the income from which is exempt from income tax.

Kind of obligation.	Amount of principal.	Rate of interest.	Amount of interest paid.
	$		$
Total	$		Amt.

7. (a) TAXES PAID.

Taxes paid or accrued on the books of the corporation during the taxable year, are deductible with the following exceptions: Federal income and excess profits taxes (including taxes paid on the interest on its own obligations in pursuance of a covenant contained therein reflecting the policy of liability for such taxes), foreign taxes on income derived from sources within the United States by foreign corporations, local taxes specially assessed against property on account of benefits derived from public improvements or betterments, and taxes upon the corporation's capital stock in the hands of the stockholders.

BASIS OF RETURN.

Is this form made on the basis of actual receipts and disbursements? .....

If not, describe fully what other basis or method was used in computing net income .....

UNDISTRIBUTED INCOME, SURPLUS, AND UNDIVIDED PROFITS.

Total net income of taxable year preceding that for which this return is made (less income tax paid thereon)	$ 62995.02
Amount of such income remaining undistributed six months after the close of that year	62995.02
Amount of such income remaining undistributed twelve months after the close of that year	62995.02
Total surplus and undivided profits at close of taxable year	18763.51

If sufficient space is not provided for the entry of any information required in the "Supplementary Statement," schedules in the form indicated, marked with the number of the item to be explained, should be attached to this form.

aa

EXHIBIT P 5

Form 1120—UNITED STATES INTERNAL REVENUE.

CORPORATION EXCESS PROFITS TAX RETURN

(Do not write in this space.)
RECEIVED
Month | Day | Year
Audited by

If necessary, ask your Collector of Internal Revenue for assistance.

For the calendar year 1917, or fiscal year beginning December 31st, 1917.

Name Detroit Can Company

Business address 120 Broadway Newport City

Kind of business Manufacture of Sheet Metal and Wire Package and Container Date established May 17th, 1902.

2752835

GENERAL INSTRUCTIONS.

39h

1. **Complete instructions.**—For complete instructions concerning the filling of this return see Regulations No. 41 relative to the War Excess Profits Taxes imposed by the War Revenue Act approved October 3, 1917, referred to hereinafter as Excess Profits Tax Regulations. Copies can be obtained from any collector of internal revenue.

2. **Who must make a return on Form 1103.**—Every corporation having for the taxable year a net income of $3,000 or more (see Form 1031) must make a return on this form of its average invested capital during the taxable year and compute the amount of its excess profits tax, if any, as directed herein.

This return should be made at the same time and in the same manner as the return of net income for the taxable year on Form 1031.

A corporation which claims that it employs in its business only a nominal capital or that it can not satisfactorily determine the amount of its invested capital must, nevertheless, fill this form as far as practicable in order to show the facts necessary for action on its claim.

3. **Taxable year.**—The taxable year is the calendar year 1917 or (if the fiscal year of the corporation differs from the calendar year) the fiscal year ending in the calendar year 1917. A corporation whose fiscal year differs from the calendar year may also use this form for its return (without entries for prewar period) covering the fiscal year ending in 1918.

4. **Taxable income.**—All the income of a corporation from whatever source derived is deemed to be derived from its business and all such income subject to the income tax is also subject to the excess profits tax except as provided for in Schedule I.

5. **Deduction.**—Each corporation whose income (derived from a business carried on with invested capital) is subject to excess profits tax may deduct from the amount of its taxable income (1) an amount equal to not less than 7 per cent and not more than 9 per cent of the amount of its invested capital, as explained below, and (2) $3,000.

If the corporation was not in existence during the whole of at least one of the calendar years 1911, 1912, and 1913, designated by the act of October 3, 1917, as the prewar period, and has not succeeded to the conduct of a business which was carried on during any one or more of those years, the first deduction is an amount equal to 8 per cent of the amount of invested capital. Otherwise the deduction is an amount equal to the same percentage of the invested capital for the taxable year as the average net income during the prewar period was of the average invested capital during that period, provided that if such percentage is less than 7 per cent, the deduction shall be computed at the rate of 7 per cent and if more than 9, at the rate of 9 per cent (see Excess Profits Tax Regulations, Article 21).

In order to take advantage of this provision, the corporation must make a return of invested capital during the prewar period as well as during the taxable year. Space for such a return is provided on this form.

If the corporation prefers, it may compute the deduction at the rate of 7 per cent and avoid the necessity of rendering a return of invested capital for the prewar period. In any case the average amount of invested capital during the taxable year must be determined if possible.

6. **Invested capital.**—For definition of "invested capital" and complete instructions for computing its amount see Excess Profits Tax Regulations, Articles 42 to 65.

7. **Computation of tax for fiscal year, part of which falls in the calendar year 1917.**—The tax of a corporation whose fiscal year differs from the calendar year shall be that proportion of the tax computed on the net income for the fiscal year which the number of months from January 1, 1917, to the end of the fiscal year bears to the entire number of months in the fiscal year.

8. **Corporations making claim for assessment under Article 82** of the Regulations (section 210 of the act of October 3, 1917) should answer all questions and fill all schedules so far as possible and attach a statement explaining why it is impracticable or in the case of foreign corporations, unreasonably expensive to fill out the entire return.

SCHEDULE I.—NET INCOME FOR TAXABLE YEAR SUBJECT TO EXCESS PROFITS TAX.

1. Net income for taxable year shown in Item 8, Form 1031		$ 1044876 62
2. Plus interest on obligations of the United States issued since September 24, 1917, held by corporation in excess of $5,000 par value		
3. TOTAL		1044876 62
4. Less (a) Dividends received, as shown in Item 9, Form 1031	$	
5. (b) Interest paid (not in excess of legal limit) on indebtedness incurred for purchase of obligations reported in item 2, above		
6. NET INCOME SUBJECT TO EXCESS PROFITS TAX		$ 1044876 62

SCHEDULE II.—INVESTED CAPITAL.

ITEM.	1911	1912	1913	TAXABLE YEAR.
1. Capital, surplus, and undivided profits at the close of the preceding year as shown by corporation's books before making any adjustments therein (from Schedule A)	$	$	$	$
2. Adjustments by way of additions (from Schedule B)				
3. TOTAL	$	$	$	$
4. Adjustments by way of deductions (from Schedule C)				
5. Invested capital at beginning of year (Item 3 less Item 4)	$	$	$	$
6. Changes in invested capital during year (from Schedules D and E)				
7. Invested capital for year	$	$	$	$
8. TOTAL INVESTED CAPITAL FOR PREWAR PERIOD				$

SCHEDULE III.—DEDUCTION.

1. Percentage—net income to invested capital for prewar period. (Item 8, Schedule F, divided by Item 8, Schedule II. Carry out result as far as desired, but drop the remainder, if any, without increasing the last figure of the percentage		$
2. Percentage to be used in computing deduction (see Instruction 5)		$
3. Amount of deduction computed at above rate on invested capital for taxable year	$	
4. Specific deduction (except for foreign corporations)		$ 9,000 00
5. TOTAL DEDUCTION	$	

SCHEDULE IV.—COMPUTATION OF TAX.

COMPUTATION OF TAX. Net income shown	Amount of income in each class.	Deduction (if in excess of 15 per cent of invested capital, enter only 15 per cent on first line and balance on line or lines below).	Balance subject to tax.	Rate.	AMOUNT OF TAX.
60 %	$	$	$	20 %	$
15 % of invested capital				25 %	
20 % of invested capital				35 %	
25 % of invested capital				45 %	
25 % of invested capital				60 %	
TOTAL	$	$	$		$

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EXHIBIT P 5

This corporation is a subsidiary corporation of the American Can company, the latter company owning the entire capital stock and the excess profit tax return is included in the consolidated return of the American Can Company, filed at the office of the Collector of Internal Revenue, Second District, Custom House, New York, N. Y.

SCHEDULE A.—CAPITAL, SURPLUS, AND UNDIVIDED PROFITS AS SHOWN BY BOOKS BEFORE MAKING ANY ADJUSTMENTS THEREIN.

A1. Stock actually outstanding (not in the corporation treasury) at the end of the preceding taxable year may be counted as invested capital to the extent that it is paid up.

A2. Reserves consisting of amounts not deductible in the computation of net income under the income tax law, may, if properly explained, be included as part of the surplus for the purpose of computing the invested capital.

ITEM.	1911	1912	1913	TAXABLE YEAR
Capital stock paid up and actually outstanding at the close of the preceding year (not including treasury stock):				
1. First preferred	$	$	$	$
2. Second preferred				
3. Common				
4. TOTAL	$	$	$	$
Surplus and undivided profits:				
5. Paid-in surplus	$	$	$	$
6. Earned surplus				
7. Undivided profits				
8. GRAND TOTAL OF ITEMS 4, 5, 6, AND 7	$	$	$	$

SCHEDULE B.—ADJUSTMENTS BY WAY OF ADDITIONS.

B1. If any part of the interest on the corporation's permanent indebtedness was excluded as a deduction from the corporation's income for any year (see Form 1031), a proportionate part of such indebtedness may be added to invested capital for that year as Item 1, Schedule B.

B2. If any addition to invested capital is reported in Item 2, Schedule B, submit a full statement showing the kind of property, the date when paid in, its value on that date, and how the value was determined.

B3. If an addition to invested capital is reported in Item 3, Schedule B, submit a statement showing the kind of property, its cost, and the year in which it was acquired.

B4. If any addition to invested capital is reported in Item 4, Schedule B, state specifically the amount of depreciation or depletion written off each year in the books of the company and the amount allowed as a deduction in computing taxable income.

ITEM.	1911	1912	1913	TAXABLE YEAR
1. Portion of permanent indebtedness, the interest on which is not deductible from income in computing income tax (Article 44)	$	$	$	$
2. Value of tangible property in excess of par value of stock issued therefor (Article 43)				
3. Additions to capital account allowable under Article 64				
4. Depreciation charged in accounts of corporation but disallowed by Treasury Department as expense on income tax returns				
5.				
6.				
7. TOTAL	$	$	$	$

SCHEDULE C.—ADJUSTMENTS BY WAY OF DEDUCTIONS.

C1. Is any good will, trade-mark, trade brand, franchise, or similar intangible property, paid in for stock, entered on the books of the corporation at a value in excess of its [illegible] at the amount of the par value of the stock issued therefor? _____ In excess (in the aggregate) of 20 per cent of the par value of the stock outstanding on March 3, 1917? _____

If so, submit a statement showing (*a*) date of acquisition; (*b*) cash value at that date; (*c*) par value of stock issued therefor; (*d*) par value of total stock outstanding on March 3, 1917; and (*e*) value at which the assets are entered on the books of the corporation.

The amount by which "*e*" exceeds "*b*," "*c*," or 20 per cent of "*d*," whichever is lowest, must be entered as Item 1, Schedule C, for the taxable year and for each year of the prewar period that is affected.

C2. Is any patent or copyright, paid in for stock, entered on the books of the corporation at a value in excess of its actual cash value when paid in? _____ In excess of the par value of the stock issued therefor? _____

If so, submit a statement showing (*a*) date of acquisition; (*b*) cash value of the patent or copyright at that date; (*c*) par value of the stock issued therefor; and (*d*) value at which the patent or copyright is entered on the books of the corporation.

The amount by which "*d*" exceeds "*b*" or "*c*," whichever is the lower, must be entered as Item 2, Schedule C, for the taxable year and for each year of the prewar period that is affected.

C3. Is any tangible property, paid in for stock, entered on the books of the corporation at a value in excess of its actual cash value when received? _____ In excess of the par value of the stock paid therefor? _____

Is any tangible property paid for specifically with stock before January 1, 1914, entered on the books of the corporation at a value in excess of its actual cash value on that date? _____

If the answer to any of the foregoing questions is "yes," submit a statement showing (*a*) kind of property; (*b*) when acquired; (*c*) par value of the stock paid therefor; (*d*) actual cash value of the property when paid in; (*e*) actual cash value of the property on January 1, 1914, if paid in before that date; (*f*) basis of the valuation stated under "*e*"; (*g*) value at which the property is entered on the corporation's books; and (*h*) amount by which such value exceeds the allowable value under Article 55 of the Excess Profits Tax Regulations. Enter this amount as Item 3, Schedule C, for the taxable year and for each year of the prewar period that is affected. (Note that the value January 1, 1914, does not affect the prewar period.)

C4. (*a*) Was any stock issued by the corporation ever returned as a gift or for a consideration substantially less than its par value? _____ (*b*) If so, what was the par value of such stock? _____ (*c*) What amount of cash or its equivalent was derived from the resale of such stock? $_____

The excess of "*b*" over "*c*" must be entered as Item 4, Schedule C, for the taxable year and for each year of the prewar period that is affected.

C5. Was the business reorganized or consolidated, or was its ownership changed after March 3, 1917? _____ If so, answer the following questions:

(*a*) Did an interest in the business of 50 per cent or more remain in the control of the same persons, corporations, associations, or partnerships, or of any of them?

(*b*) Were any of the assets entered on the books of the corporation making this return at a higher value than on the books of its predecessor? _____

(*c*) If so, were such assets paid for specifically as such in cash or tangible property? _____

The increase in book value of any property not so paid for must be deducted from the invested capital for the taxable year as Item 5, Schedule C, unless it can be shown that under the excess profits law and regulations the property was undervalued on the books of the predecessor business.

C6. Is any property paid for with cash or with other tangible property entered on the books of the corporation at a value in excess of the amount of cash paid therefor or the actual cash value of the tangible property paid therefor? _____ If so, submit a statement showing (*a*) kind of property; (*b*) amount of cash paid therefor; (*c*) actual cash value of other tangible property paid therefor; (*d*) how that value was determined; (*e*) value at which the property is entered on the books of the corporation; and (*f*) excess of "*e*" over "*b*" or "*c*." This excess must be entered as Item 6, Schedule C, for the taxable year and for each year of the prewar period that is affected.

C7. Has adequate provision been made in the expense accounts of the company for (*a*) losses of every kind? _____; (*b*) depreciation? _____; (*c*) obsolescence? _____; (*d*) depletion of mineral deposits, timber supplies and the like? _____

If adequate charge has not been made for depreciation, depletion, obsolescence, and other losses, and the value of the property has not been maintained by replacements that have been charged to expense, proper additional charges for depreciation must be computed for all years in which they were not made on the books, and the total amount of such charges must be entered as Item 7, Schedule C, for the taxable year (and for each year of the prewar period that was affected) and deducted in arriving at its surplus and undivided profits.

C8. Has the corporation any stocks, bonds (other than obligations of the United States), or other assets, the income from which is not subject to excess profits tax? _____ If so, at what value are they carried on the corporation's books? $_____ Has any portion of such assets been included in invested capital in accordance with Articles 45 and 46 of the Excess Profits Tax Regulations? _____ If so, how much? $_____ Is the balance in excess of the corporation's indebtedness, excluding the amount thereof that has been included in invested capital as Item 1, Schedule B? _____ If so, state the amount of such excess. $_____

Enter this amount as Item 8 in Schedule C, for the taxable year, and make a similar correction for each year of the prewar period.

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SCHEDULE C.—ADJUSTMENTS BY WAY OF DEDUCTIONS (Continued).

ARTICLE (LIST OF AMOUNT OF)	1913	1914	1915	1916
1. Valuation of good will, trade-marks, trade brands, franchises, or other intangible property purchased with stock (Articles 37 and 38)				
2. Valuation of patents and copyrights paid in for stock (Article 38)				
3. Valuation of tangible property paid in for stock (Article 38)				
4. Stock returned to corporation as a gift, etc. (Article 39)				
5. Valuation of assets acquired in reorganizations (Article 40)				
6. Appreciation (Article 42)				
7. Depreciation and depletion (Article 43)				
8. Excess of stocks and other intangible assets over indebtedness (Article 44)				
9.				
10.				
11. TOTAL DEDUCTIONS				

SCHEDULE D.—CHANGES IN INVESTED CAPITAL DURING TAXABLE YEAR.

Specify (by using red ink for distributions, or otherwise) whether each item represents an addition or a distribution.

Report dividends paid out of profits of prior years but not dividends paid out of profits of the taxable year.

In column 4 enter the number of whole months remaining in the year, plus a fraction consisting of the number of days remaining in the month (including the date of change) divided by the total number of days in the month.

Assets (other than cash) paid in for stock, must be valued in accordance with Articles 36 to 39 of the Excess Profits Tax Regulations.

Nature of additions and distributions	Year.	Amount.	Number of months remaining.	Adjusted change. (Column 3 × column 4.)
1.				
2.				
3.				
4.				
5.				
6.				
7.				
8.				
9. NET ADDITION OR REDUCTION				

SCHEDULE E.—CHANGES IN INVESTED CAPITAL DURING PREWAR PERIOD.

See instructions under Schedule D. Complete one addition or reduction schedule for each year.

Nature of additions and distributions	Year.	Amount.	Number of months.	Adjusted change. (Column 3 × column 4.)
1.				
2.				
3.				
4.				
5.				
6.				
7.				
8.				
9.				
10.				
11.				
12.				
13.				
14.				
15.				
16.				
17.				
18.				

SCHEDULE F.—NET INCOME DURING PREWAR PERIOD.

ITEM.	1912	1913	1914
1. Net income for year as reported on income tax return. (Do not include figures for less than a whole year's income)			
2. Plus amount of Federal income tax paid during year			
3. TOTAL for each year			
4. Less amount of dividends received in 1913			
5. NET TOTAL for year 1913			
6. GRAND TOTAL FOR PREWAR PERIOD			

BB3

EXHIBIT P 5

QUESTIONS.

1. Explain the nature of the corporation's business if not adequately described on first page:
   (a) Main business [illegible]
   (b) Collateral businesses, if any [illegible]

2. Date of incorporation May 17th 1902. 3. Under the laws of what State or country? New Jersey

4. Enter on the following lines the names and addresses of three representative concerns in your locality engaged in the same kind of business:
   [illegible]

5. What was the fair value of the total capital stock of the corporation as determined in the last assessment of the capital stock tax (if any)? Specify the year.

6. If any patent is included among your assets, attach a schedule to this return showing for each patent its serial number, date of issue, name of patentee, amount of cash or stock paid therefor, and its present book value.

7. If the corporation ever took over a going business or otherwise acquired a mixed aggregate of tangible property, patents, and copyrights, and good will and other similar intangible property, and paid for such property in whole or in part with stock or other securities, submit a statement showing—
   (a) The name of the concern taken over (or from which the property was acquired).
   (b) The nature of the assets and liabilities so acquired.
   (c) The total par value of the stock issued therefor.
   (d) The value at which each class of assets was carried on the books of the concern from which acquired. (If obtainable submit a balance sheet of the predecessor corporation as at the date of acquisition.)
   (e) The value at which each item was entered on the books of the corporation making this return. The different classes of property must be valued as prescribed by Article 59 of the Excess Profits Tax Regulations and the values so obtained must be used in making adjustments 1, 2, and 3, Schedule C.

   If patents or copyrights were acquired, state the basis on which their value was determined, and how they were paid for.

   If good will or other intangible assets were acquired, state the basis on which their value was determined, and how they were paid for.

8. Is the corporation affiliated with one or more other corporations within the meaning of Article 77 of the Excess Profits Tax Regulations? _____ If so, submit a statement describing all its intercorporate relationships.

39-h

9. Is this return a consolidated return within the meaning of Article 78 of the Excess Profits Tax Regulations? _____ If so, submit a schedule showing in detail the computation of the consolidated invested capital and income.

10. If the corporation was not in existence during the whole of any one of the calendar years 1911–1913, is its business substantially a continuation of a business carried on during any one or more of those years? _____ If so, give name under which, and address at which, its business was then carried on.

11. Submit a copy, in detail, of—
   (a) The balance sheet of the corporation at the beginning of the taxable year.
   (b) The balance sheet of the corporation at the close of the taxable year.

We, the undersigned, president and treasurer of the above-named company, being severally duly sworn, each for himself deposes and says that the foregoing return, including the accompanying schedules and statements (if any), has been examined by him and is to the best of his knowledge and belief a true and complete return made in good faith pursuant to the Excess Profits Tax Regulations.

Sworn to and subscribed before me this 29th day of March, 1918

Seal of officer taking affidavit.

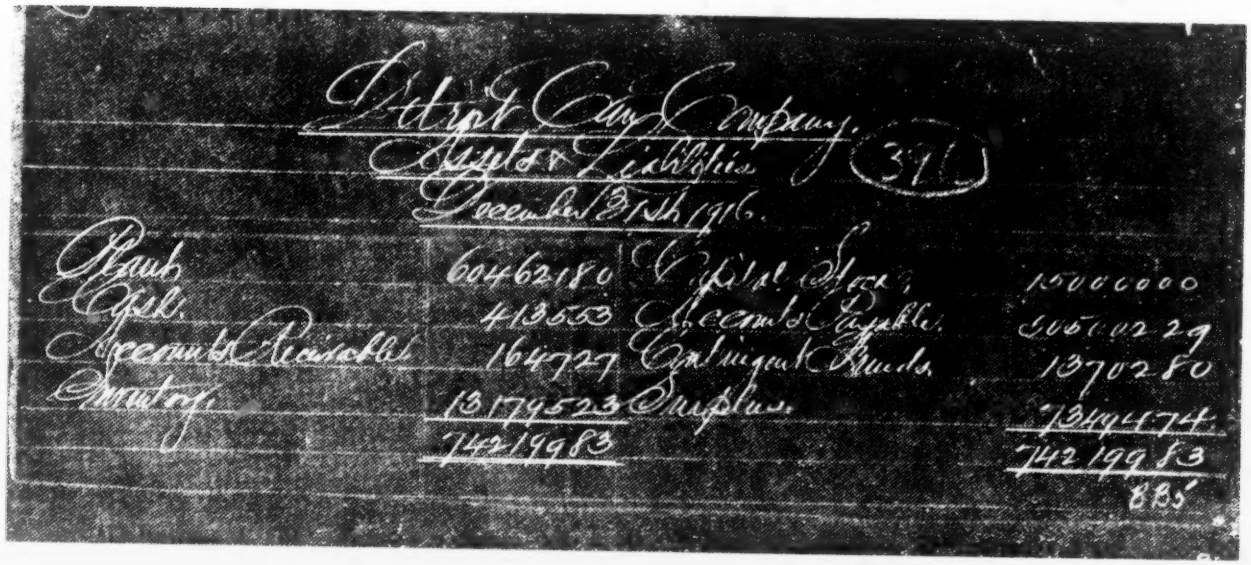
William A. Fuller
Notary Public
(Official capacity.)

G. H. Welles, President.

R. D. Moore, Treasurer.

BBy

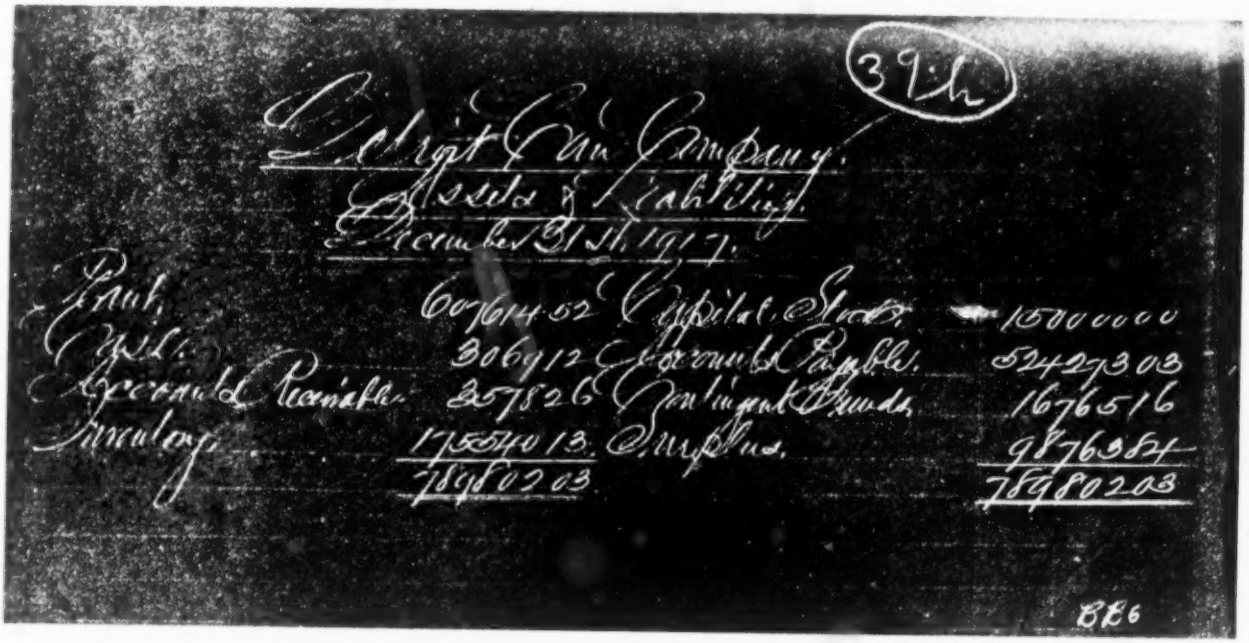
EXHIBIT P 5



Detroit City Company.
Assets & Liabilities
December 31st 1916.

Assets	60462180	Capital Stock	15000000
Cash	413653	Accounts Payable	6056029
Accounts Receivable	164727	Contingent Funds	1370280
Inventory	13179523	Surplus	13494774
	74219983		74219983

885



Lehigh Coal Company
Assets & Liabilities
December 31st, 1917.

Bank
Cash
Accounts Receivable
Inventory

60,761452 Capital Stock
306912 Accounts Payable
257826 Contingent Funds
1755340 13 Surplus

15000000
5242303
1676516
9876954

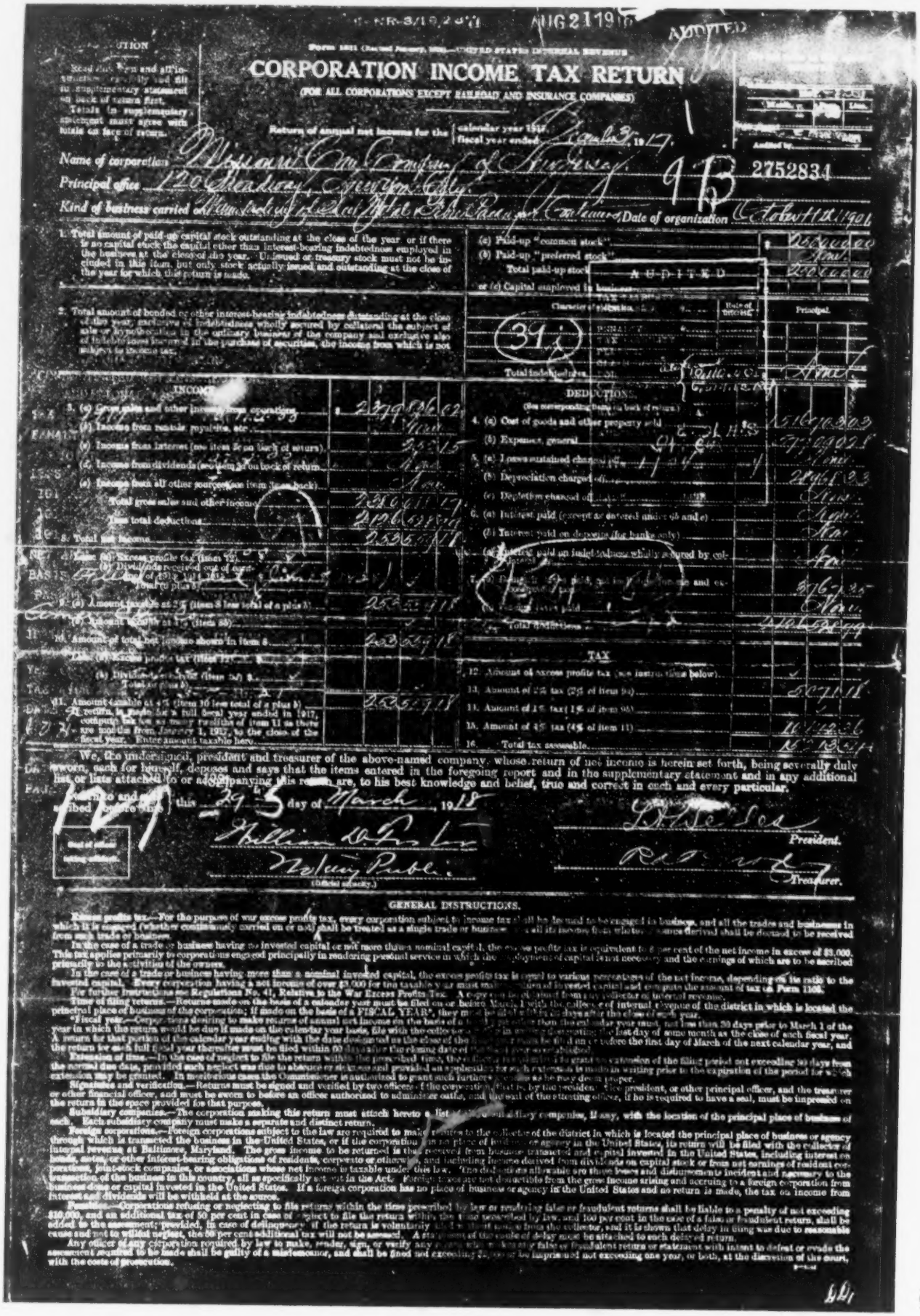
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BB6

39-h

EXHIBIT P-5



Form 1031 (Revised January, 1918)—UNITED STATES INTERNAL REVENUE

CORPORATION INCOME TAX RETURN

(FOR ALL CORPORATIONS EXCEPT RAILROAD AND INSURANCE COMPANIES)

AUDITED

AUG 21 1918

2752834

Return of annual net income for the { calendar year 1917, fiscal year ended March 31, 1917.

Name of corporation Missouri Car Foundry Co. of Kansas

Principal office 120 Broadway, Granite City, Ill.

Kind of business carried on Manufacturing Steel Underframe Cars

Date of organization October 11th 1901

AUDITED

1. Total amount of paid-up capital stock outstanding at the close of the year or if there is no capital stock the capital other than interest-bearing indebtedness employed in the business at the close of the year. Unissued or treasury stock must not be included in this item, but only stock actually issued and outstanding at the close of the year for which this return is made.

(a) Paid-up "common stock" $ 200,000.00

(b) Paid-up "preferred stock" 200,000.00

Total paid-up stock

or (c) Capital employed in business

2. Total amount of bonded or other interest-bearing indebtedness outstanding at the close of the year, exclusive of indebtedness wholly secured by collateral the subject of sale or hypothecation in the ordinary business of the company and exclusive also of indebtedness incurred for the purchase of securities, the income from which is not subject to excise tax.

Character of indebtedness	Rate of interest	Principal
(31)		
Total indebtedness		None

INCOME

3. (a) Gross sales and other income from operations		$ 2379,996.02
(b) Income from rentals, royalties, etc.		None
(c) Income from interest (see item 2 on back of return)		95.15
(d) Income from dividends (see item 3 on back of return)		None
(e) Income from all other sources (see item 4 on back)		None
Total gross sales and other income		2380,091.17
Less total deductions		2196,654.99
5. Total net income		2533,436.18
Less: (a) Excess profits tax (item 12)		
(b) Dividends received out of earnings of 1916 and 1917 (item 6)		
Taxable net income (item 7)		2533,436.18
8. (a) Amount taxable at 2% (item 7 less total of a plus b)		2533,436.18
(b) Amount taxable at 4% (item 7 less $5,000)		
9. Amount of total net income shown in item 8		2533,436.18
Less: (a) Excess profits tax (item 12)		
(b) Dividends received (item 6)		
Total (item 9)		
11. Amount taxable at 2% (item 10 less total of a plus b)		2533,436.18

If return is made for a full fiscal year ended in 1917, compute tax on as many results of item 11 as there are months from January 1, 1917, to the close of the fiscal year. Enter amount taxable here.

DEDUCTIONS

(See corresponding items on back of return)

4. (a) Cost of goods and other property sold		2116,738.03
(b) Expenses, general		77,892.28
5. (c) Losses sustained charged off		None
(d) Depreciation charged off		2196.83
(e) Depletion charged off		None
6. (a) Interest paid (except as entered under (b) and (c))		None
(b) Interest paid on deposits (for banks only)		None
(c) Interest paid on indebtedness wholly secured by collateral		None
7. Taxes paid, not including income and excess profits taxes		376.25
Other deductions		None
Total deductions		2196,654.99

TAX

12. Amount of excess profits tax (see instructions below)	
13. Amount of 2% tax (2% of item 9a)	50,668.72
14. Amount of 3% tax (3% of item 9b)	
15. Amount of 4% tax (4% of item 11)	101,374.36
16. Total tax assessable	152,043.08

We, the undersigned, president and treasurer of the above-named company, whose return of net income is herein set forth, being severally duly sworn, each for himself, deposes and says that the items entered in the foregoing report and in the supplementary statement and in any additional list or lists attached to or accompanying this return are, to his best knowledge and belief, true and correct in each and every particular.

Sworn to and subscribed before me this 29th day of March, 1918

William D. Forsyth

Notary Public.

(Official capacity.)

(Seal of officer taking affidavit.)

D. D. Lee

President.

R. [illegible]

Treasurer.

GENERAL INSTRUCTIONS.

Excess profits tax.—For the purpose of war excess profits tax, every corporation subject to income tax shall be deemed to be engaged in business, and all the trades and businesses in which it is engaged (whether continuously carried on or not) shall be treated as a single trade or business, and all its income from whatever source derived shall be deemed to be received from such trade or business.

In the case of a trade or business having no invested capital or not more than a nominal capital, the excess profits tax is equivalent to 8 per cent of the net income in excess of $3,000. This tax applies primarily to corporations engaged principally in rendering personal service in which the employment of capital is not necessary and the earnings of which are to be ascribed primarily to the activities of the owners.

In the case of a trade or business having more than a nominal invested capital, the excess profits tax is equal to various percentages of the net income, depending on its ratio to the invested capital. Every corporation having a net income of over $3,000 for the taxable year must make a return of invested capital and compute the amount of tax on Form 1338.

For further instructions see Regulations No. 41, Relative to the War Excess Profits Tax. A copy can be obtained from any collector of internal revenue.

Time of filing returns.—Returns made on the basis of a calendar year must be filed on or before March 1 with the collector of internal revenue of the district in which is located the principal place of business of the corporation; if made on the basis of a FISCAL YEAR, they must be filed within 60 days after the close of such year.

Corporations desiring to make returns of annual net income on the basis of a fiscal year other than the calendar year must, not less than 30 days prior to March 1 of the year in which the return would be due if made on the calendar year basis, file with the collector of internal revenue a request stating the last day of some month as the close of such fiscal year. A return for that portion of the calendar year ending with the date designated as the close of the fiscal year must be filed on or before the first day of March of the next calendar year, and the return for each full fiscal year thereafter must be filed within 60 days after the closing date of the fiscal year established.

Extension of time.—In the case of neglect to file the return within the prescribed time, the collector may grant an extension of the filing period not exceeding 30 days from the normal due date, provided such neglect was due to absence or sickness and provided an application for such extension is made in writing prior to the expiration of the period for which extension may be granted. In meritorious cases the Commissioner is authorized to grant such further extensions as he may deem proper.

Signatures and verification.—Returns must be signed and verified by two officers of the corporation, that is, by the president, vice president, or other principal officer, and the treasurer or other financial officer, and must be sworn to before an officer authorized to administer oaths, and the seal of the attesting officer, if he is required to have a seal, must be impressed on the return in the space provided for that purpose.

Subsidiary companies.—The corporation making this return must attach hereto a list of all subsidiary companies, if any, with the location of the principal place of business of each. Each subsidiary company must take a separate and distinct return.

Foreign corporations.—Foreign corporations subject to the law are required to make returns to the collector of the district in which is located the principal place of business or agency through which it transacted the business in the United States, or if the corporation has no place of business or agency in the United States, its return will be filed with the collector of internal revenue at Baltimore, Maryland. The gross income to be returned is that received from business transacted and capital invested in the United States, including interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise, and including income derived from dividends on capital stock or from net earnings of resident corporations, joint-stock companies, or associations whose net income is taxable under this law. The deductions allowable are those losses and disbursements incident and necessary to the transaction of the business in this country, all as specifically set out in the Act. Foreign taxes are not deductible from the gross income arising and accruing to a foreign corporation from business done or capital invested in the United States. If a foreign corporation has no place of business or agency in the United States and no return is made, the tax on income from interest and dividends will be withheld at the source.

Penalties.—Corporations refusing or neglecting to file returns within the time prescribed by law or rendering false or fraudulent returns shall be liable to a penalty of not exceeding $10,000, and an additional tax of 50 per cent in case of neglect to file the return within the time prescribed by law, and 100 per cent in the case of a false or fraudulent return, shall be added to the assessment; provided, in case of delinquency if the return is voluntarily made without notice from the collector, and it is shown that delay in filing was due to reasonable cause and not to willful neglect, the 50 per cent additional tax will not be assessed. A statement of the cause of delay must be attached to such delayed return.

Any officer of any corporation required by law to make, render, sign, or verify any return who makes any false or fraudulent return or statement with intent to defeat or evade the assessment required to be made shall be guilty of a misdemeanor, and shall be fined not exceeding $10,000 or be imprisoned not exceeding one year, or both, at the discretion of the court, with the costs of prosecution.

EXHIBIT P 6

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SUPPLEMENTARY STATEMENT

The following information must be furnished, either on this sheet or on attached schedules, by every corporation, joint-stock company, or association. Without such information the returns will not be accepted as complete. The items below relate to the correspondingly numbered items

[illegible]

[illegible] for the purpose of the income tax (including [illegible] securities owned by the corporation except interest [illegible] or political subdivision thereof or interest upon the obligations of the [illegible] or any corporation.

5. (c) FROM DIVIDENDS RECEIVED.

Any distribution made or ordered to be made by a corporation out of its earnings or profits accrued since March 1, 1913, whether in cash or stock of the paying company, must be returned (under Items 5 (c) on front page of this form) by the receiving corporation as income of that year in which the distribution was made or ordered to be made and will be taxed at the rate prescribed by law for the years in which surplus or profits distributed were earned. Thus, if an amount received out of earnings of 1913 (subsequent to March 1, 1913), and 1914, and 2% on amounts received from earnings of 1916 and 1917. A statement from the corporation paying the dividends included herein should be attached to this return, showing what part of the amount of dividends paid out of earnings of each year mentioned is taxable. Such will be deemed to have been paid out of the earnings of 1917 and will be taxed at 2%. The receiving corporation, in order that tax may be computed on the basis prescribed in 1917 on the rates applicable to the years in which the profits were earned, must fill in the following form:

Dividends received in 1917 out of profits earned each year subsequent to March 1, 1913.

1913	1914	1915	1916	1917	Total.
$	$	$	$	$	$

5. (c) FROM OTHER SOURCES.

Income received from all sources not elsewhere specified should be itemized below:

	$			
Total	$	None.		

6. (a) COST OF GOODS AND OTHER PROPERTY SOLD.

Report the cost of goods sold in the following form:

Merchandise bought for sale	$		
Cost of manufacture of articles, materials, parts, or supplies shown on books. (Explain on schedule in following portion)		1612	77 77
Less withdrawals for use		67	07 96
Total		1545	69 81
Less inventory at end of year		127	94 40
Net cost of goods sold		1417	75 41

Explain:

If the corporation carries inventories of merchandise or materials, explain the basis on which they are made, whether (a) at cost, or (b) at cost or market value, whichever is lower. If no inventories are made, make no entries referring to inventories, but report the total cost of goods purchased or produced during the year. If the cost of manufacturing or otherwise producing goods is not kept separate from general expenses in the corporation's accounts, include such cost in "Expenses, general," below.

Explain fully in a separate schedule any case in which any corporation that has sold any of its [illegible] during the year should report the cost of the property sold [illegible]

Kind of property.

2. Market value March 1, 1913, if acquired before that date.

3. Cost of subsequent improvements, if any.

4. Depreciation and depletion to date of sale.

5. Net [illegible] (Item 1 or Item 2 plus Item 3 minus Item 4).

State how market value March 1, 1913, was determined.

Does such value include any paid-in? If so, how much? $

6. (b) EXPENSES, GENERAL.

This item should include only the ordinary and necessary expenses paid within the year in the operation of the business and maintenance of the properties of the corporation, itemized as per schedule below. It must not include any expenditures reported under 4 (a), 5, 6, or 7.

Expenditures for incidental repairs which do not add to the value or appreciably prolong the life of property are deductible as expenses, but expenditures for new buildings, permanent improvements or betterments which increase the value of property, or for restoring or replacing property, are not deductible under this or any other item of the return. Such expenditures for property chargeable to capital account, to be extinguished through annual depreciation charges.

Payments made to officers or employees, who are stockholders, in the guise of salaries or compensation, the amount of which is based upon the stockholdings of such officers or employees, are not deductible as a business expense.

1. Salaries of officers	$	1832 76
2. Salaries, wages (not deducted in "Cost of manufacture, or otherwise reported under 4 (a))		2744 25 11
3. Rent		720 00
4. Repairs, taxes and insurance		4462 84
Operating Expenses		9722 61
Amount		1455 65 11
	$	21 937 02

If any item of deduction in this return represents payments you paid to others, state the amount, the name and address of the recipient, and the reason therefor.

[illegible]

7. (a) LOSSES.

All losses sustained during the year must be distinguished from depreciation or allowances for exhaustion, wear and tear. The losses not compensated by insurance or otherwise, sustained during the year, and charged off on the

Kind of property.	Cost of property.	Cause of loss.	Amount charged off within year.
	$		$
	$		None.

When was the property acquired?

How was the property acquired?

The cost of property lost, destroyed or demolished was $

A bad debt of sufficient amount accrued since January 1, 1913, will not be allowed as a deduction unless the amount was reported as income for the year in which the debt was created.

State how the debts charged off (if any) were ascertained to be worthless.

If at any future time a debt charged off as worthless is collected the amount collected must be returned as income in the year in which received.

Unpaid debts are not deductible if made good by recovery of property sold or situation of property pledged.

39.

8. (b) DEPRECIATION.

The amount deductible on account of depreciation is an amount *charged off* which fairly measures the loss during the year in the value of physical property by reason of exhaustion, wear, and tear. Such amount should be determined upon the basis of the cost of the property and the probable number of years constituting its life. Stocks, bonds, and like securities, as well as any other intangible assets, are not subject to exhaustion, wear and tear within the meaning of the law. Hence any amount charged off as representing a *shrinkage* in the value of such assets is not deductible either as depreciation or as a loss.

Depreciation computed on total invoice value of merchandise in stock is not an allowable deduction by reason of damage or obsolescence the merchandise is unsalable.

If a deduction is made on account of depreciation, the following statement must be filled in:

Kind of property.	Its cost.	Probable life after acquirement.	Amount of depreciation charged off. This year.	Previous years.
Building*	332974	10 Years	33297	99892
Machinery	51 1650	outfitted	1706 50	5119 50
Total	384624	years	35003 50	105011 50

* If building, state under "Kind of property" the material of which constructed.

8. (c) DEPLETION.

Depletion applies to the exhaustion of natural deposits, and contemplates a deduction to return to the corporation the capital invested, or in case of purchase prior to March 1, 1913, an amount sufficient to return to the corporation the fair market price or value of such deposits as of that date. An allowable deduction on account of depletion must not exceed the fair market value as of March 1, 1913, or the cost subsequent to that date, of the product mined and sold during the year, and will be determined in accordance with the rule set out in Articles 170 to 178, Regulations 33, Revised. The amount sought to be deducted on this account must be charged off on the books of the company.

Kind of property.	Its cost if acquired subsequent to March 1, 1913.	Fair market value as of March 1, 1913.	Amount of depletion charged off. This year.	Previous years.
	$	$	$	$
			None.	

* Name from what source, coal or ore, etc.

† State how the market value as of March 1, 1913, was determined.

9. INTEREST PAID.

(a) The amount of interest deductible under (c) is the amount actually paid within the year on an amount of bonded or other indebtedness (except on indebtedness falling under 6 (b) or 6 (c) and indebtedness incurred for the purchase of obligations or securities the income from which is exempt from income tax) not in excess of the paid-up capital stock outstanding at the close of the year, or if there is no capital stock, the entire amount of capital (not including interest-bearing indebtedness) employed in the business at the close of the year, plus, in each case, one-half of the interest-bearing indebtedness also then outstanding.

Capital employed in the business, as here used, contemplates the entire capital paid in by the members of the company, including so much of the accumulated surplus as is actually employed in the business, but does not include any borrowed capital or interest-bearing indebtedness.

(b) Interest paid (by banks) on deposits or on money received for investment and secured by interest-bearing certificates of indebtedness issued by a bank, banking association, or loan or trust company is deductible in the entire amount so paid.

(c) If the corporation's indebtedness, or any part thereof, is wholly secured by collateral which is the subject of sale or hypothecation in the corporation's ordinary business as a dealer in such property, the interest paid on an amount of such indebtedness not exceeding the actual value of the collateral may be deducted.

Describe all obligations on which interest is paid in the following form. Distinguish plainly collateral loans falling under 6 (c) and also obligations incurred for the purchase of securities, the income from which is exempt from income tax.

Kind of obligation.	Amount of principal.	Rate of interest.	Amount of interest paid.
	$		$
Total	$		None.

7. (a) TAXES PAID.

Taxes, paid or accrued on the books of the corporation during the taxable year, are deductible with the following exceptions: Federal income and excess profits taxes (including taxes paid on the interest on its own obligations in pursuance of a covenant contained therein following the letter of the law for such taxes), foreign taxes on income derived from sources within the United States by foreign corporations, local taxes specially assessed against property on account of benefits derived from public improvements or betterments, and taxes upon the corporation's capital stock in the hands of the stockholders.

BASIS OF RETURN.

Is this return made on the basis of actual receipts and disbursements? Yes.

If not, describe fully what other basis or method was used in computing net income.

UNDISTRIBUTED INCOME, SURPLUS, AND UNDIVIDED PROFITS.

Total net income of taxable year preceding that for which this return is made (less income tax paid thereon)	$ 55806.21
Amount of such income remaining undistributed six months after the close of that year	55806.21
Amount of such income remaining undistributed twelve months after the close of that year	55806.21
Total surplus and undivided profits at close of taxable year	195905.37

If sufficient space is not provided for the entry of any information required in the "Supplementary Statement," schedules in the form indicated, marked with the number of the item to be explained, should be attached to this form.

DD2

EXHIBIT P 6

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SCHEDULE A.—CAPITAL, SURPLUS, AND UNDIVIDED PROFITS AS SHOWN BY BOOKS BEFORE MAKING ANY ADJUSTMENTS UNDER

A4. Stock actually outstanding (not in the corporation treasury) at the end of the year. Amount of taxable year may be counted as invested capital to the extent that it is paid up.

Reserves consisting of amounts not deductible in the computation of net income.

ITEM.	1917.	1918.	1919.	TAXABLE YEAR.
[illegible] outstanding at the close of the preceding year				
[illegible]				
[illegible]				
[illegible]

SCHEDULE C.—ADJUSTMENTS BY WAY OF DEDUCTIONS (Concluded). Page 4

STATEMENT OF ACCOUNT OF (For corresponding taxable year see page 2)	1917	1918	1919
1. Valuation of good-will, trade-marks, trade brands, franchises, or other intangible property purchased with stock (Articles 57 and 58)			
2. Valuation of patents and copyrights paid in for stock (Article 58)			
3. Valuation of tangible property paid in for stock (Article 58)			
4. Stock returned to corporation as a gift, etc. (Article 54)			
5. Valuation of assets acquired in reorganizations (Article 50)			
6. Appreciation (Article 42)			
7. Depreciation and depletion (Article 42)			
8. Excess of stocks and other inadmissible assets over indebtedness (Article 44)			
9.			
10.			
11. TOTAL DEDUCTIONS			

SCHEDULE D.—CHANGES IN INVESTED CAPITAL DURING TAXABLE YEAR.

Specify (by using red ink for distributions, or otherwise) whether each item represents an addition or a distribution.

Report dividends paid out of profits of prior years, but not dividends paid out of profits of the taxable year.

In column 4 enter the number of whole months remaining in the year, plus a fraction consisting of the number of days remaining in the month (including the date of change) divided by the total number of days in the month.

Assets (other than cash) paid in for stock, must be valued in accordance with Articles 58 to 60 of the Excess Profits Tax Regulations.

Nature of additions and distributions.	Date.	Amount.	Number of months (plus fraction)	Adjusted average. (Column 3 × column 4 ÷ 12)
1	2	3	4	5
1.				
2.				
3.				
4.				
5.				
6.				
7.				
8.				
9. NET ADDITION OR REDUCTION				

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SCHEDULE E.—CHANGES IN INVESTED CAPITAL DURING PREWAR PERIOD.

See instructions under Schedule D. Compute net addition or reduction separately for each year.

Nature of additions and distributions.	Date.	Amount.	No. of months (plus fraction)	Adjusted average. (Column 3 × column 4 ÷ 12)
1	2	3	4	5
1.				
2.				
3.				
4.				
5.				
6.				
7.				
8.				
9.				
10.				
11.				
12.				
13.				
14.				
15.				
16.				
17.				
18.				

SCHEDULE F.—NET INCOME DURING PREWAR PERIOD.

ITEM.	1913	1918	1919
1. Net income for year as reported on income tax return. (Do not include figures for less than a whole year's business)			
2. Plus amount of Federal income tax paid during year			
3. TOTAL for each year			
4. Less amount of dividends received in 1913			
5. NET TOTAL for year 1913			
6. GRAND TOTAL FOR PREWAR PERIOD			

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EXHIBIT P 9

QUESTIONS.

1. Explain the nature of the corporation's business if not adequately described on first page:
   (a) Main business [illegible]
   (b) Collateral businesses, if any None

2. Date of incorporation [illegible] 3. Under the laws of what State or country? New Jersey

4. Enter on the following lines the names and addresses of three representative concerns in your locality engaged in the same kind of business [illegible]

5. What was the fair value of the total capital stock of the corporation as determined in the last assessment of the capital stock tax (if any)? Specify the year

6. If any patent is included among your assets, attach a schedule to this return showing for each patent its serial number, date of issue, name of patentee, amount of cash or stock paid therefor, and its present book value

7. If the corporation ever took over a going business or otherwise acquired a mixed aggregate of tangible property, patents, and copyrights, and good will and other similar intangible property, and paid for such property in whole or in part with stock or other securities, submit a statement showing—
   (a) The name of the concern taken over (or from which the property was acquired).
   (b) The nature of the assets and liabilities so acquired.
   (c) The total par value of the stock issued therefor.
   (d) The value at which each class of assets was carried on the books of the concern from which acquired. (If obtainable submit a balance sheet of the predecessor corporation as at the date of acquisition.)
   (e) The value at which each item was entered on the books of the corporation making this return. The different classes of property must be valued as prescribed by Article 59 of the Excess Profits Tax Regulations and the values so obtained must be used in making adjustments 1, 2, and 3, Schedule C.
   If patents or copyrights were acquired, state the basis on which their value was determined, and how they were paid for.
   If good will or other intangible assets were acquired, state the basis on which their value was determined, and how they were paid for.

8. Is the corporation affiliated with one or more other corporations within the meaning of Article 77 of the Excess Profits Tax Regulations? ..... If so, submit a statement describing all its intercorporate relationships.

9. Is this return a consolidated return within the meaning of Article 78 of the Excess Profits Tax Regulations? ..... If so, submit a schedule showing in detail the computation of the consolidated invested capital and income.

10. If the corporation was not in existence during the whole of one of the calendar years 1911, 1912, and 1913, is its business substantially a continuation of a business carried on during any one or more of those years? ..... If so, give the name under which, and address at which, its business was then carried on

11. If, in addition to the balance sheet of the corporation at the beginning of the taxable year,
   (a) The balance sheet of the corporation at the close of the taxable year.

We, the undersigned, president and treasurer of the above-named company, being severally duly sworn, each for himself deposes and says that the foregoing return, including the accompanying schedules and statements, has been examined by him and is to the best of his knowledge and belief a true and complete return made in good faith pursuant to the Excess Profits Tax Regulations.

Sworn to and subscribed before me this 29th day of March, 1918

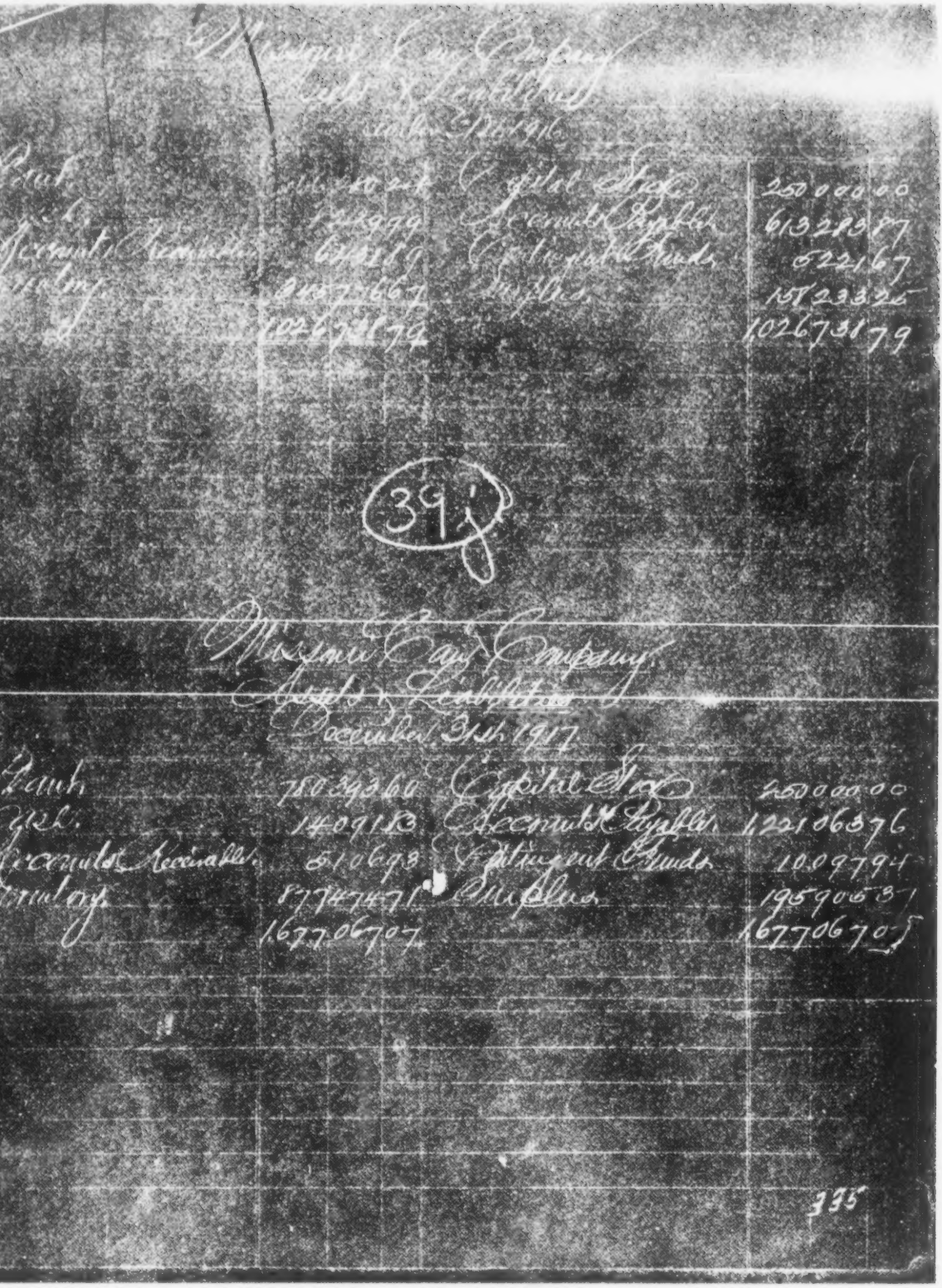
William A. Pinkerton
Notary Public
(Official signature.)

L. A. Welles
President.

R. A. Long
Treasurer.

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EXHIBIT P 6



Missouri Cap Company
Assets & Liabilities
December 31st 1916

Cash	780,393.60	Capital Stock	250,000.00
U.S.	140,918.13	Accounts Payable	613,218.87
Accounts Receivable	610,698	Contingent Funds	22,167
Inventory	877,467.71	Surplus	187,233.25
	1,677,067.07		1,677,067.07

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Missouri Cap Company
Assets & Liabilities
December 31st 1917

Cash	780,393.60	Capital Stock	250,000.00
U.S.	140,918.13	Accounts Payable	1,221,063.76
Accounts Receivable	610,698	Contingent Funds	10,097.94
Inventory	877,467.71	Surplus	195,906.31
	1,677,067.07		1,677,067.07

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EXHIBIT P-6

Mr. HENDLER. Your Honor may not need our argument after receiving the printed briefs.

Mr. HENDLER. I move for judgment for the defendant.

The COURT. Motion denied.

Exception allowed and sealed.

[SEAL.] J. L. BODINE.

128 *Exhibit P–7*

American Can Company and American subsidiaries

Calculation of consolidated net income for 1917 on cash basis

Net income:		
American Can Company	$12,673,359.76	
Missouri Can Company	124,164.87	
Detroit Can Company	6,556.48	
American Can Company of Massachusetts	45,709.93	
American Can Company of Utah	56,474.07	
Sanitary Can Company	104,107.84	
Chas. W. Shonk Company	80,559.91	
Newton Manufacturing Company	34,228.19	
Raleigh Manufacturing Company	15,670.15	
Union Can Company	8,768.52	
Total		$13,149,599.72
Net losses:		
Davenport Can Company		71.46
Aggregate net income		13,149,528.26
Deduct:		
Dividends received by American Can Company from domestic corporations		60,010.50
Consolidated net income for excess profits tax		13,089,517.76

129 ## American Can Company

Calculation of net income for 1917 on cash basis

Gross amount of income received in 1917		$116,786,504.27
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$101,310,074.96	
2. Losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise	1,722,851.27	
3. Interest on indebtedness paid in 1917, (not including any indebtedness for purchase of obligations or securities the interest on which was exempt from Federal income tax)	744,340.27	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	335,878.01	
Total deductions		104,113,144.51
Net income for 1917 on cash basis		12,673,359.76
Deduct:		
Dividends received from domestic corporations		60,010.50
Net income for 4% tax		12,613,349.26

130 American Can Company

Calculation of gross income for 1917 on cash basis

Cash received by treasurer in 1917 as per treasurer's cash books		$131,285,302.02
Add cash received by agents in 1917 recorded in treasurer's cash books in 1918		56,290.90
		131,341,592.92
Deduct cash received by agents in 1916 recorded in treasurer's cash books in 1917	$64,881.48	
Deduct other cash advanced to agents and returned by agents to treasurer in 1917	43,234.31	
		108,115.79
Total cash received by company in 1917		131,233,477.13
Deduct nonincome items		14,446,972.86
Gross amount of income received by company in 1917		116,786,504.27

131 American Can Company

Schedule of nonincome items of cash received in 1917

Borrowed money repaid to company by Canadian subsidiaries and money borrowed by company from Canadian subsidiaries	$3,102,846.37
Borrowed money repaid to company by American subsidiaries	3,272.98
Money borrowed by company	8,824,000.00
Borrowed money repaid to company by Lissberger	6,000.00
Proceeds of sale of bonds of company (less profit)	1,814,658.96
Proceeds of sale of Liberty bonds to employees	235,151.73
Proceeds of sale of Liberty bonds to others	408,053.03
Payments on account of fire loss of equipment	44,589.82
Proceeds of sale of equipment	8,400.00
Total of nonincome items	$14,446,972.86

132 Missouri Can Company

Calculation of net income for 1917 on cash basis

Gross amount of cash received in 1917 as per treasurer's cash books		$1,005,779.96
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$848,978.95	
2. Losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise	28,968.33	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	3,667.81	
Total deductions		881,615.09
Net income for 1917 on cash basis		$124,164.87

133 Detroit Can Company

Calculation of net income for 1917 on cash basis

Gross amount of income received in 1917		$241,246.48
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$211,806.34	
2. Losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise	16,352.21	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	6,531.45	
Total deductions		234,690.00
Net income for 1917 on cash basis		$6,556.48

134 Detroit Can Company

Calculation of gross income for 1917 on cash basis

Cash received by treasurer in 1917 as per treasurer's cash books	$260,246.48
Deduct receipts on account of sale of real estate (no profit)	19,000.00
Gross amount of income received by company in 1917	$241,246.48

135 American Can Company of Massachusetts

Calculation of net income for 1917 on cash basis

Gross amount of cash received in 1917 as per treasurer's cash books		$1,656,891.07
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$1,579,659.60	
2. Losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise	25,704.62	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	5,816.92	
Total deductions		1,611,181.14
Net income for 1917 on cash basis		$45,709.93

136 American Can Company of Utah

Calculation of net income for 1917 on cash basis

Gross amount of income received in 1917		$1,642,967.13
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$1,556,307.95	

Deductions—Continued.		
2. Losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise	$27,101.80	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	3,083.31	
Total deductions		$1,586,493.06
Net income for 1917 on cash basis		$56,474.07

137 American Can Company of Utah

Calculation of gross income for 1917 on cash basis

Cash received by treasurer in 1917 as per treasurer's cash books	$1,637,775.10
Add cash received by agents in 1917 recorded in treasurer's cash books in 1918	17,136.20
	$1,654,911.30
Deduct cash received by agents in 1916 recorded in treasurer's cash books in 1917	11,944.17
Gross amount of income received by company in 1917	$1,642,967.13

138 Sanitary Can Company

Calculation of net income for 1917 on cash basis

Gross amount of income received in 1917		$1,765,362.29
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$1,592,331.58	
2. Losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise	60,049.93	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	8,872.94	
Total deductions		1,661,254.45
Net income for 1927 on cash basis		$104,107.84

139 Sanitary Can Company

Calculation of gross income for 1917 on cash basis

Cash received by treasurer in 1917 as per treasurer's cash books	$1,766,362.29
Deduct cash advanced to agents and returned by agents to treasurer in 1917	1,000.00
Gross amount of income received by company in 1917	$1,765,362.29

140 C. W. Shonk Company

Calculation of net income for 1917 on cash basis

Gross amount of income received in 1917		$1,555,359.38
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$1,422,680.75	
2. Losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise	46,546.39	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	5,572.23	
Total deductions		1,474,799.47
Net income for 1917 on cash basis		$80,559.91

141 C. W. Shonk Company

Calculation of gross income for 1917 on cash basis

Cash received by treasurer in 1917 as per treasurer's cash books		$1,551,685.38
Add cash received in 1917 and not passed through treasurer's cash books		10,407.68
		$1,562,093.06
Deduct cash advanced to agents and returned by agents to treasurer in 1917	$5,233.68	
Deduct cash deposited by company as earnest money and returned to company in 1917	1,500.00	
		6,733.68
Gross amount of income received by company in 1917		$1,555,359.38

142 Newton Manufacturing Company

Calculation of net income for 1917 on cash basis

Gross amount of cash received in 1917 as per treasurer's cash books		$939,065.87
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$901,405.96	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	3,431.72	
Total deductions		904,837.68
Net income for 1917 on cash basis		34,228.19

143 RALEIGH MANUFACTURING COMPANY

Calculation of net income for 1917 on cash basis

Gross amount of income received in 1917		$166,615.59
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$150,838.89	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	106.55	
Total deductions		150,945.44
Net income for 1917 on cash basis		$15,670.15

144 RALEIGH MANUFACTURING COMPANY

Calculation of gross income for 1917 on cash basis

Cash received by treasurer in 1917 as per treasurer's cash books	$168,845.59
Deduct cash advanced to agents and returned by agents to treasurer in 1917	2,230.00
Gross amount of income received by company in 1917	166,615.59

145 UNION CAN COMPANY

Calculation of net income for 1917 on cash basis

Gross amount of cash received in 1917 as per treasurer's cash books		$173,565.24
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$155,789.26	
2. Losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise	6,500.00	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits	2,507.46	
Total deductions		164,796.72
Net income for 1917 on cash basis		8,768.52

146 DAVENPORT CAN COMPANY

Calculation of net income for 1917 on cash basis

Gross amount of cash received in 1917 as per treasurer's cash books		$5,133.50
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$3,967.04	
4. Taxes paid in 1917 (not including income or excess profits taxes imposed by authority of the United States or taxes assessed against local benefits)	1,237.92	
Total deductions		5,204.96
Net income for 1917 on cash basis		71.46

147 *Exhibit P–8*

Exhibit P–8
1–13–27

American Can Company year ended December 31, 1917

Consolidated net income, cash basis

Net income:		
American Can Company	$12,673,359.76	
Missouri Can Company	124,164.87	
Detroit Can Company	6,556.48	
American Can Company of Massachusetts	45,709.93	
American Can Company of Utah	56,474.07	
Sanitary Can Company	104,107.84	
Chas. W. Shonk Company	80,559.91	
Newton Manufacturing Company	34,228.19	
Raleigh Manufacturing Company	15,670.15	
Union Can Company	8,768.52	
Total		$13,149,599.72
Net losses:		
Davenport Can Company		71.46
Aggregate net income		13,149,528.26
Deduct:		
Dividends received by American Can Company from domestic corporations		60,010.50
Consolidated income for excess-profits tax purposes		13,089,517.76

148 American Can Company year ended December 31, 1917

Consolidated invested capital as amended by Internal Revenue Department letter March 7, 1921		$60,348,919.50
Consolidated net income, cash basis		13,089,517.76
	Income	Tax
Deduction, 9% $5,431,402.76 plus $3,000.00	$5,434,402.76	
Taxable @ 20%	3,617,935.17	723,587.03
25%	3,017,445.98	754,361.50
35%	1,019,733.85	356,906.85
	13,089,517.76	1,834,855.38

Allocation of excess-profits tax

American Can Company 100%	$1,834,855.38

Computation of total tax

Net income (cash basis)	$12,673,359.76	
Deduct:		
Excess profits tax	1,834,855.38	
		Tax
Taxable @ 2%	10,838,504.38	$216,770.09
Less dividends from 1916 and 1917 earnings	60,010.50	
Taxable @ 4%	10,778,493.88	431,139.76
Excess-profits tax as above		1,834,855.38
Total tax		2,482,765.23
Tax paid prior to March 7, 1921		5,219,980.65
Excess tax paid prior to March 7, 1921		2,737,215.42

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Missouri Can Company

December 31, 1917

Computation total tax, cash basis

		Tax
Net income	$124,164.87	
Deduct excess-profits tax	None.	
Taxable @ 2%	124,164.87	$2,483.30
Taxable @ 4%	124,164.87	4,966.59
Total tax		7,449.89
Tax paid prior to March 7, 1921		15,213.54
Excess tax paid prior to March 7, 1921		7,763.65

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Detroit Can Company

December 31, 1917

Computation total tax, cash basis

		Tax
Net income	$6,556.48	
Deduct excess-profits tax	None.	
Taxable @ 2%	6,556.48	$131.13
Taxable @ 4%	6,556.48	262.26
Total tax		393.39
Tax paid prior to March 7, 1921		6,287.19
Excess tax paid prior to March 7, 1921		5,893.80

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Exhibit P–9

P–9
5–16–27

American Can Company and American subsidiaries

Calculation of consolidated net income for 1917 on cash basis (revised)

Net income:		
American Can Company	$12,754,886.02	
Missouri Can Company	124,164.87	
Detroit Can Company	6,556.48	
American Can Company of Massachusetts	45,709.93	
American Can Company of Utah	56,474.07	
Sanitary Can Company	104,107.84	
Chas. W. Shonk Company	80,559.91	
Newton Manufacturing Company	34,228.19	
Raleigh Manufacturing Company	15,670.15	
Union Can Company	8,768.52	
Total		$13,231,125.98
Net losses:		
Davenport Can Company		71.46
Aggregate net income		13,231,054.52
Deduct:		
Dividends received by American Can Company from domestic corporations		60,010.50
Consolidated net income for excess-profits tax		13,171,044.02

152 P–9–a

American Can Company

Calculation of net income for 1917 on cash basis (revised)

Gross amount of income received in 1917		$116,786,504.27
Deductions:		
1. Ordinary and necessary expenses paid in 1917 in the maintenance and operation of business and properties	$101,310,074.96	
2. Losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise	1,641,325.01	
3. Interest on indebtedness paid in 1917 (not including any indebtedness for purchase of obligations or securities the interest on which was exempt from Federal income tax)	744,340.27	
4. Taxes paid in 1917 (not including income or excess-profits taxes imposed by authority of the United States or taxes assessed against local benefits)	335,878.01	
Total deductions		104,031,618.25
Net income for 1917 on cash basis		12,754,886.02
Deduct:		
Dividends received from domestic corporations		60,010.50
Net income for 4% tax		12,694,875.52

153 *Exhibit P–10*

P–10

Computation of American Can Company taxes for 1917

Computation excess-profits tax

Consolidated invested capital as fixed in commissioner's letter of March 7, 1921		$60,348,919.50
Consolidated net income on cash receipt & disbursement basis (as revised)		$13,171,044.02
	Income	Tax
9% invested capital plus $3,000.00	$5,434,402.76	0
Taxable @ 20%	3,617,935.17	$723,587.03
" " 25%	3,017,445.98	754,361.50
" " 35%	1,101,260.11	385,441.04
	$13,171,044.02	$1,863,389.57

Allocation excess-profits tax American Can Company 100%

Computation total tax

Net income of American Can Company on cash receipt & disbursement basis (as revised)	$12,754,886.02	
Deduct excess-profits tax	1,863,389.57	
Taxable @ 2%	$10,891,496.45	$217,829.93
Less dividends	60,010.50	
Taxable @ 4%	10,891,485.95	433,259.44
Excess-profits tax as above		1,863,389.57
Total taxes		$2,514,478.94
Amount collected by Edwards prior to March 7, 1921		5,219,980.65
Amount wrongfully collected		$2,705,501.71

154 *Exhibit P–11*

P–11

American Can Company and American subsidaries, net income for 1917 as returned

Net income		
American Can Company	$16,927,404.35	
Missouri Can Company	253,559.18	
Detroit Can Company	104,786.64	
American Can Company of Massachusetts	313,885.46	
American Can Company of Utah	133,007.24	
Sanitary Can Company	8,330.14	
Chas. W. Shonk Company	269,024.23	
Total		$18,009,997.24
Net losses		
Union Can Company	8,706.17	
Davenport Can Company	4,430.48	
Newton Manufacturing Company	1,127.57	
Raleigh Manufacturing Company	0	
Wade Machine Company	1,332.56	
Total		15,596.78
Aggregate net income		$17,994,400.46
Deduct:		
Dividends received by American Can Company from domestic corporations		60,010.50
Consolidated net income for excess-profits tax purposes		$17,934,389.96

155 P–10

American Can Company, taxes for 1917 based on income as returned

Computation of excess-profits tax

Consolidated invested capital as fixed in commissioner's letter of March 7, 1921		$60,348,919.50
Consolidated net income as returned		17,934,389.96
	Income	Tax
Deduction, 9%, $5,431,402.76 plus $3,000.00	$5,434,402.76	
Taxable @ 20%	3,617,935.17	$723,587.03
@ 25%	3,017,445.98	754,361.50
@ 35%	3,017,445.98	1,056,106.09
@ 45%	2,847,160.07	1,281,222.03
	$17,934,389.96	$3,815,276.65

Allocation of excess-profits tax

American Can Company 100%	$3,815,276.65

Computation of total tax

		Tax
Net income of American Can Company as returned	$16,927,404.35	
Deduct Excess-profits tax	3,815,276.65	
Taxable @ 2%	$13,112,127.70	$262,242.55
Less dividends received from domestic corporations	60,010.50	
Taxable @ 4%	13,052,117.20	522,084.69
Excess-profits tax as above		3,815,276.65
		$4,599,603.89
Amount collected by Edwards prior to March 7, 1921		5,219,980.65
Excess		$620,376.76

156 *Exhibit D–1*

D–1

Memorandum in answer to letter of assistant U. S. attorney to Judge Treacy, dated April 4, 1927

All figures are consolidated figures for American Can Company and all American subsidaries.

1. The quantities and cost of tin plates on hand and in process January 1, 1917, were as follows:

On hand	1,287,850 bb.	$4,507,016.68
In process	212,425 bb.	$1,369,259.41

2, 3, and 4. The quantities of tin plates purchased at $3.60 per base box during each month of 1917 were as follows:

January	355,277 bb.
February	147,715 "
March	117,244 "
April	42,595 "
May	404 "
June	846 "
July	950 "
August	10,550 "
September	7,939 "
October	8,555 "
November	0 "
December	0 "
Total	692,075 "

5 and 6. The quantities of tin plates purchased during 1917 at $7 per base box was approximately 4,102,236 bb. This plate was all purchased during months of July to December, inclusive.

7. The quantities of tin plate on hand and in process on December 31, 1917, were as follows:

On hand	1,987,937 bb.
In process	228,226 bb.

D–2
5–16–27

Exhibit D–2

American Can Company and subsidiaries—statement showing consolidated net income as reported on return

	American Can Co. of N. J.	Missouri Can Co.	Detroit Can Co.	American Can Co. of Mass.	American Can Co. of Utah	Sanitary Can Co.	Chas. W. Shonk Co.
Gross sales	$89,721,248.72	$2,379,836.02	$622,401.55	$2,078,684.14	$1,392,532.16	$8,917,067.10	$1,730,989.61
Less: Cost of sales	58,861,819.06	1,516,703.03	333,616.99	1,334,954.32	1,076,444.04	7,754,888.06	619,652.27
Gross profit	30,859,429.66	863,132.99	288,784.56	737,749.82	316,088.12	1,162,179.04	1,111,337.34
Other income:							
Rentals	2,295.02		141.72				
Interest	348,946.29	252.15	4,009.93	554.06	2,397.51		
Dividends received	60,010.50						
Income—munitions dept	4,089,013.95						
Royalties—Pacific American fisheries	82,462.25						
Profit on bonds redeemed	13,607.75						
Miscellaneous profits	92,611.35			315.82	864.13	24,813.68	
Gross income	35,548,376.77	863,385.14	292,936.21	744,619.70	319,349.76	1,186,992.72	1,111,337.34
Deductions:							
Officer's salaries	358,786.81	13,337.85	3,556.76	11,559.47	5,335.14	32,900.03	4,400.00
Labor and wages	9,986,724.81	377,475.81	114,463.22	238,009.58	95,427.75	654,416.78	456,545.30
Rentals	127,543.24	770.00	50.00	18,899.91		137.00	1,385.04
Repairs	1,060,712.76	44,694.87	14,388.66	33,722.61	13,540.64	117,401.55	92,883.52
Operating expenses	2,537,866.80	97,226.61	23,307.29	64,222.46	27,179.31	178,464.45	134,378.07
General expenses	1,039,413.85	43,585.14	9,321.98	32,798.67	14,674.57	125,327.77	88,586.96
Losses:							
Sale of British bonds	41,782.51						
Sale of Liberty bonds	14,366.00						
Bad debts	41,396.27			1,801.62	12,101.80	353.88	1,546.39
Depreciation	2,209,377.79	28,968.33	16,352.21	23,903.00	15,000.00	59,713.67	45,000.00
Interest paid	812,974.40						14,545.63
Domestic taxes	288,280.44	3,767.35	6,709.45	5,816.92	3,083.31	9,947.44	4,742.20
Foreign taxes	41,746.64						
Contingent fund							
Total deductions	18,620,972.42	609,825.96	188,149.57	430,734.24	186,342.52	1,178,662.58	842,313.11
Net income	16,927,404.35	253,559.18	104,786.64	313,885.46	133,007.24	8,330.14	269,024.23

	Union Can Co.	Davenport Can Co.	Newton Mfg. Co.	Raleigh Mfg. Co.	Wade Machine Co.	Consolidated
Gross sales	$714,050.20		$3,796,803.54	$868,120.89	$101,984.27	$112,323,723.20
Less: Cost of sales	607,464.42		3,075,315.85	293,499.46		75,474,337.50
Gross profit	106,585.78		721,492.69	574,621.43	101,984.27	36,849,385.70
Other income:						
Rentals						2,436.74
Interest					160.44	336,320.38
Dividends received						60,010.50
Income—munitions dept						4,989,013.96
Royalties—Pacific American fisheries						82,462.25
Profit on bonds redeemed						13,607.75
Miscellaneous profits	596.78					119,201.76
Gross income	107,182.56		721,492.69	574,621.43	102,144.71	41,572,439.03
Deductions:						
Officer's salaries	3,112.16		61,351.10		4,664.06	499,003.38
Labor and wages	54,816.08	$3,145.88	345,906.07		69,234.35	12,394,165.63
Rentals			8,036.59		2,100.00	158,921.78
Repairs	8,511.01		37,629.46		15,302.86	1,438,788.04
Operating expenses	28,488.08		102,577.22		5,113.67	3,198,823.97
General expenses	11,953.94		109,202.59	574,621.43	7,062.33	2,056,849.23
Losses:						
Sale of British bonds						41,782.51
Sale of Liberty bonds						14,366.00
Bad debts						57,199.96
Depreciation						2,519,320.51
Interest paid	6,500.00		54,505.51			827,520.03
Domestic taxes						329,504.21
Foreign taxes	2,507.46	1,237.92	3,411.72			41,746.64
Contingent fund		46.68				46.68
Total deductions	115,888.73	4,430.48	722,620.26	574,621.43	103,477.27	23,578,038.57
Net income	8,706.17	4,430.48	1,127.57		1,332.56	17,994,400.46
Deduct: Dividends						60,010.50
Consolidated net income for excess-profits tax purposes as originally reported on return						17,934,389.96

Exhibit D–3

Exhibit D–3
5–16–27

American Can Company and Subsidiary—Statement showing consolidated net income as amended

	American Can Co. of N. J.	Missouri Can Co.	Detroit Can Co.	American Can Co. of Mass.	American Can Co. of Utah	Sanitary Can Co.	Chas. W. Shank Co.
Gross sales	$89, 721, 248. 72	$2, 379, 836. 02	$622, 401. 55	$2, 078, 684. 14	$1, 392, 532. 16	$8, 917, 067. 10	$1, 730, 989. 61
Less: Cost of sales	54, 139, 319. 06	1, 348, 203. 03	263, 616. 99	1, 143, 434. 32	1, 025, 444. 04	7, 291, 888. 06	619, 652. 27
Gross profit	35, 581, 929. 66	1, 031, 632. 99	358, 784. 56	935, 249. 82	367, 088. 12	1, 625, 179. 04	1, 111, 337. 34
Other income:							
Rentals	2, 295. 02		141. 72				
Interest	348, 946. 29	252. 15	4, 009. 93	554. 06	2, 397. 51		
Dividends received	60, 010. 50						
Income—Munitions defit	4, 556, 003. 64						
Royalties—Pacific American Fisheries	82, 462. 25						
Profit on bonds redeemed	13, 607. 75						
Miscellaneous profits	92, 611. 35			315. 82	864. 13	24, 813. 68	
Gross income	40, 737, 866. 46	1, 031, 885. 14	362, 936. 21	936, 119. 70	370, 349. 76	1, 649, 992. 72	1, 111, 337. 34
Deductions:							
Officer's salaries	358, 786. 81	13, 337. 85	3, 556. 76	11, 559. 47	5, 335. 14	32, 900. 03	4, 400. 00
Labor and wages	9, 986, 724. 81	377, 475. 81	114, 463. 22	238, 009. 58	95, 427. 75	654, 416. 78	454, 545. 30
Rentals	127, 543. 24	770. 00	50. 00	18, 899. 91		137. 00	1, 395. 04
Repairs	1, 060, 712. 86	44, 694. 87	14, 388. 66	33, 722. 61	13, 540. 64	117, 401. 55	92, 883. 52
Operating expenses	2, 537, 866. 80	97, 226. 61	23, 307. 29	64, 222. 46	27, 179. 31	178, 464. 46	134, 378. 07
General expenses	898, 713. 85	43, 585. 14	9, 321. 98	32, 798. 67	14, 674. 57	125, 327. 77	88, 886. 96
Losses:							
Sale of British bonds	41, 782. 51						
Sale of Liberty bonds	14, 366. 00						
Bad debts	41, 396. 27			1, 801. 62	12, 101. 80	353. 38	1, 546. 39
Depreciation	1, 113, 252. 09	28, 968. 33	16, 352. 21	25, 903. 00	15, 000. 00	59, 713. 67	45, 000. 00
Interest paid	812, 974. 40						14, 545. 63
Domestic taxes	698, 374. 46	3, 767. 35	6, 709. 45	5, 816. 92	3, 083. 31	9, 947. 44	4, 742. 20
Foreign taxes	41, 746. 64						
Discount on bonds	70, 000. 00						
Total deductions	17, 804, 240. 74	609, 825. 96	188, 149. 57	430, 734. 24	186, 342. 52	1, 178, 662. 58	842, 313. 11
Net income	22, 933, 625. 72	422, 059. 18	174, 786. 64	505, 385. 46	184, 007. 24	471, 330. 14	269, 024. 23

	Union Can Co.	Davenport Can Co.	Newton Can Co.	Raleigh Mfg. Co.	Wade Machine Co.	Consolidated
Gross sales	$714,050.20		$3,790,808.54	$868,120.89	$101,984.27	$112,323,723.20
Less: Cost of sales	602,464.42		3,075,315.85	293,499.46		69,802,837.50
Gross profit	111,585.78		721,492.69	574,621.43	101,984.27	42,520,885.70
Other income:						
Rentals						2,436.74
Interest					160.44	356,320.38
Dividends received						60,010.50
Income—Munitions defit						4,556,003.64
Royalties—Pacific American Fisheries						82,462.25
Profit on bonds redeemed						13,607.75
Miscellaneous profits	596.78					119,201.76
Gross income	112,182.56		721,492.69	574,621.43	102,144.71	47,710,928.72
Deductions:						
Officer's salaries	3,112.16		61,351.10		4,664.06	499,003.38
Labor and wages	54,816.08	$3,145.88	345,906.07		69,234.35	12,394,165.63
Rentals			8,036.59		2,100.00	158,921.78
Repairs	8,511.01		37,629.46		15,302.86	1,438,788.04
Operating expenses	28,488.08		102,577.22		5,113.67	3,198,823.97
General expenses	11,953.94		109,202.59	574,621.43	7,062.33	1,916,149.23
Losses:						
Sale of British bonds						41,782.51
Sale of Liberty bonds						14,366.00
Bad debts						57,199.96
Depreciation	6,500.00		54,505.51			1,363,194.81
Interest paid						827,520.03
Domestic taxes	2,507.46	1,237.92	3,411.72			739,598.23
Foreign taxes						41,746.64
Discount on bonds						70,000.00
Total deductions	115,888.73	4,383.80	722,620.26	574,621.43	103,477.27	22,761,260.21
Net income	3,706.17	4,383.80	1,127.57		1,332.56	24,949,668.51
Deduct: Dividends						60,010.50
Final determination of consolidated net income for excess profits tax purposes as shown in bureau letter dated March 7, 1921						24,889,658.01

D–4 Id.

EXHIBIT A

Comparative income on cash receipts and disbursements, basis of individual companies ascertained without and with the use of inventories

American Can Company	As reported without Inventories	As amended with Inventories	Missouri Can Co.		Detroit Can Co.		American Can Co., Mass.		American Can Co., Utah	
			As reported without Inventories	As amended with Inventories	As reported without Inventories	As amended with Inventories	As reported without Inventories	As amended with Inventories	As reported without Inventories	As amended with Inventories
Gross income received	$116, 786, 504. 27	$116, 786, 504. 27	$1, 005, 779. 96	$1, 005, 779. 96	$241, 246. 48	$241, 246. 48	$1, 656, 891. 06	$1, 656, 891. 07	$1, 642, 967. 13	$1, 642, 967. 13
Less—Cost of sales and other expense										
Inventory per books—Jan. 1, 1917		9, 940, 576. 77		345, 776. 67		131, 796. 23		274, 685. 38		128, 003. 18
Adjusted—Add accts. receivable		9, 064, 497. 27		5, 417. 21		1, 379. 56		93, 742. 11		31, 391. 69
Total		19, 005, 074. 04		352, 193. 88		133, 174. 79		368, 427. 49		159, 394. 87
Adjusted—Less accts. payable		4, 636, 177. 83		43, 829. 29		10, 979. 54		28, 362. 61		8, 729. 63
Inventory amended on C. R. & D. basis		14, 368, 896. 21		307, 364. 59		122, 195. 25		340, 064. 88		150, 665. 25
Add—Cash purchases by parent transferred (*)				968, 759. 74		232, 500. 00				
Add—Cash purchases by individual companies	58, 150, 885. 82	58, 150, 885. 82	196, 186. 96	196, 186. 96	11, 217. 10	11, 217. 10	1, 016, 694. 48	1, 016, 694. 48	1, 260, 000. 00	1, 260, 000. 00
Total		72, 519, 782. 03		1, 472, 311. 29		365, 912. 35		1, 356, 759. 36		1, 410, 665. 25
Less—Inventory per books—Dec. 31, 1917		24, 373, 662. 72		1, 045, 974. 71		245, 540. 13		611, 473. 14		196, 973. 10
Adjusted—Add accounts receivable		7, 376, 522. 43		3, 591. 52		2, 479. 23		83, 973. 80		82, 947. 24
Total		31, 750, 185. 15		1, 049, 566. 23		248, 019. 36		695, 446. 94		279, 920. 34
Adjusted—Less accts. payable		10, 063, 876. 73		24, 269. 24		45, 818. 65		8, 832. 49		13, 096. 41
Inventory amended on C. R. & D. basis		21, 686, 308. 42		1, 025, 296. 99		202, 200. 71		686, 614. 45		266, 823. 93
Balance represents cost of sales on cash basis	58, 150, 885. 82	50, 833, 473. 61	196, 186. 96	447, 014. 30	11, 217. 10	163, 711. 64	1, 016, 894. 48	670, 144. 91	1, 260, 000. 00	1, 143, 841. 32
Add—Ordinary and necessary expense										

Losses	1,722,851.27	1,722,851.27	28,968.33	28,968.33	16,352.21	16,352.21	25,704.62	25,704.62	27,101.86	27,101.86
Interest	744,340.27	744,340.27								
Taxes	335,878.01	335,878.01	3,667.81	3,667.81	6,531.45	6,531.45	5,816.92	5,816.92	3,083.31	3,083.31
Total	104,113,144.51	93,074,846.35	881,615.09	1,132,442.43	234,690.00	387,184.54	1,611,181.14	1,284,631.57	1,586,493.06	1,470,334.38
Net income for 1917 on cash basis	12,673,359.76	23,711,657.92	124,164.87	(126,662.47)	6,556.48	(145,938.06)	45,709.93	392,259.50	56,474.07	172,632.75
Computation of total tax										
Net income as above	12,673,359.76	23,711,657.92	124,164.87	(126,662.47)	6,556.48	(145,938.06)	45,709.93	392,259.50	56,474.07	172,632.75
Less—Excess profits tax	1,834,855.38	6,909,531.41								
Taxable at 2%	10,838,504.38	16,802,126.51	124,164.87	(126,662.47)	6,556.48	(145,938.06)	45,709.93	392,259.50	56,474.07	172,632.75
Less—Dividends from 1916–17 earnings	60,010.50	60,010.50								
Taxable at 4%	10,778,493.88	16,742,116.01	124,164.87	(126,662.47)	6,556.48	(145,938.06)	45,709.93	392,259.50	56,474.07	172,632.75
Amount of tax at 2%	216,770.09	336,042.53	2,483.30		131.13		914.20	7,845.19	1,129.48	3,452.66
Amount of tax at 4%	431,139.76	669,684.64	4,966.59		262.26		1,828.40	15,690.38	2,258.96	6,905.31
Excess profits tax	1,834,855.38	6,909,531.41								
Total tax	2,482,765.23	7,915,258.58	7,449.89		393.39		2,742.60	23,535.57	3,388.44	10,357.97
Tax paid prior to March 7, 1921	5,219,980.65	5,219,980.65	15,213.54	15,213.54	6,287.19	6,287.19	18,833.13	18,833.13	7,980.42	7,980.42
Additional tax or refund	(2,737,215.42)	2,695,277.93	(7,763.65)	(15,213.54)	(5,893.80)	(6,287.19)	(16,090.53)	4,702.44	(4,591.98)	2,377.55
*Excluding purchases by parent for subsidiaries		3,639,359.69*								
Liberty bond adjustment		1,327.61								
Bad debts		80,198.65								
		$3,720,885.95								

Comparative income on cash receipts and disbursements, basis of individual companies ascertained without and with the use of inventories—Continued

American Can Company	Sanitary Can Co.		Union Can Co.		Davenport Can Co.		C. W. Shonk & Co.	
	As reported without Inventories	As amended with Inventories	As reported without Inventories	As amended with Inventories	As reported without Inventories	As amended with Inventories	As reported without Inventories	As amended with Inventories
Gross income received	$1,765,362.29	$1,765,362.29	$173,565.24	$173,565.24	$5,133.50	$5,133.50	$1,555,359.38	$1,555,359.38
Less—Cost of sales and other expense								582,025.61
Inventory per books—Jan. 1, 1917		956,069.57		55,444.29				179,296.09
Adjusted—Add accts. receivable		431,691.30		6,085.04				
Total		1,387,760.87		61,529.33				761,321.70
Adjusted—Less accts. payable		76,591.91		5,028.03				42,366.88
Inventory amended on C. R. & D. basis		1,311,169.06		56,501.30				718,954.82
Add—Cash purchases by parent transferred (*)		1,535,000.00		153,000.00				744,966.45
Add—Cash purchases by individual companies	95,728.14	95,728.14				5,133.50	320,592.23	320,592.23
Total		2,941,897.20		209,401.30		5,133.50		1,784,513.50
Less—Inventory per books—Dec. 31, 1917		1,927,396.01		100,339.21				821,392.32
Adjusted—Add accounts receivable		398,281.42		5,237.79				257,840.61
Total		2,325,677.43		195,577.00				1,079,232.93
Adjusted—Less accts. payable		42,291.11		2,590.30				37,664.25
Inventory amended on C. R. & D. basis		2,283,386.32		192,986.70				1,041,568.68
Balance represents cost of sales on cash basis	95,728.14	658,510.88		16,514.60		5,133.50	320,592.23	742,944.82
Add—Ordinary and necessary expense								
Mfg. & general administration expense	1,496,603.44	1,496,603.44	155,789.26	155,789.26	3,967.04	3,967.04	1,102,088.52	1,102,088.52
Losses	60,049.93	60,049.93	6,500.00	6,500.00			46,546.39	46,546.39
Interest								
Taxes	8,872.94	8,872.94	2,507.46	2,507.46	1,237.92	1,237.92	5,572.33	5,572.33
Total	1,661,254.45	2,224,037.19	164,796.72	181,311.32	5,204.96	10,338.46	1,474,799.47	1,897,152.06
Net incom for 1917 on cash basis	104,107.84	(458,674.90)	8,768.52	(7,746.08)	(71.46)	(5,204.96)	80,559.91	(341,792.68)
Computation of total tax								

Taxable at 2%.....	104, 107. 84	(458, 674. 90)	8, 768. 52	(7, 746. 08)		(5, 204. 96)	80, 559. 91	(341, 792. 68)
Less—Dividends from 1916–17 earnings.....								
Taxable at 4%.....	104, 107. 84	(458, 674. 90)	8, 768. 52	(7, 746. 08)		(5, 204. 96)	80, 559. 91	(341, 792. 68)
Amount of tax at 2%.....	2, 082. 16		175. 37				1, 611. 20	
Amount of tax at 4%.....	4, 164. 32		350. 70				3, 222. 40	
Excess profits tax.....								
Total tax.....	6, 246. 48		526. 11				4, 833. 60	16, 141. 45
Tax paid prior to March 7, 1921.....	499. 80	499. 80					16, 141. 45	
Additional tax or refund.....	5, 746. 68	(499. 80)	526. 11				(11, 307. 85)	(16, 141. 45)

160 In United States District Court, District of New Jersey.

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

MISSOURI CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

DETROIT CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Memorandum

Filed May 31, 1927

Graham Sumner, Esq., and John J. Treacy, Esq., for the plaintiffs; Walter G. Winne, Esq., United States attorney, and Charles T. Hendler, special attorney, Internal Revenue, for the United States.

BODINE, District Judge.

161 These suits are brought to recover income taxes claimed to be improperly levied and assessed under the revenue act of 1917.

It is conceded that the court has jurisdiction, and that the action may be maintained under section 281 (a) and section 1014 of the revenue act of 1924.

The revenue act of 1917 provides that taxes shall be levied upon the income of the taxpayer determined upon the cash basis. It also provides that where the taxpayer keeps its account and makes its return upon some other basis which clearly reflects its income that the tax shall be computed upon the income returned.

Section 10 imposes a tax upon income received. Section 12 provides for certain deductions, such as expenses of business, losses, interest, and taxes.

Section 13 (d) provides, so far as pertinent, as follows:

"A corporation * * * keeping accounts upon any basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect its income, may, subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned."

The American Can Company, and its subsidiaries, made returns for the year 1917 pursuant to the statute last above quoted. The commissioner ruled that the method by which the companies valued their inventories of tin plate did not reflect their true income and reassessed the taxes.

The commissioner made certain adjustments prior to March 7, 1921, which had the effect of increasing the incomes to $19,278,121.83 (including $60,010.50 as dividends), which was $1,286,721.37 in excess of the incomes as returned and $6,047,067.31 in excess of
162 their incomes determined on the cash basis, and also had the effect of reducing their consolidated invested capital. In accordance with these changes, the commissioner made assessments against the American Can Company for additional income and excess-profits taxes and the American Can Company paid, and Edwards collected, the amounts of such assessments prior to March 7, 1921.

The amounets of the income and excess-profits taxes for 1917 which were so paid by the plaintiffs and the dates of payment thereof were as follows:

American Can Company

June 14, 1918, under original return	$3,266,499.86
November 22, 1919, under additional assessment	520,762.54
September 21, 1920, under additional assessment	1,432,718.25
	$5,219,980.65

Missouri Can Company

June 14, 1918, under original return	$15,213.54

Detroit Can Company

June 14, 1918, under original return	$6,287.19

If the taxes were computed upon the incomes of the plaintiffs determined on the cash basis, they would be as follows:

American Can Company	$2,514,478.94
Missouri Can Company	7,449.89
Detroit Can Company	393.39
Total	$2,522,322.22

The amounts which the plaintiffs seek to recover in these suits, being the amounts paid to Edwards, collector, prior to March 7, 1921, in excess of the amounts which were legally payable, are as follows:

American Can Company, $2,705,501.71, with interest at the rate of 6% per annum on $1,432,718.25 from September 21, 1920,
163 on $520,762.54 from November 22, 1919, and on $752,020.92 from June 14, 1918.

Missouri Can Company, $7,763.65, with interest at the rate of 6% per annum from June 14, 1918.

Detroit Can Company, $5,893.80, with interest at the rate of 6% per annum from June 14, 1918.

It is thus to be noted that the taxpayer made its return pursuant to the discretionary provision contained in section 13 (d) of the act. The commissioner, who up to this time had not issued any regulations with respect to the valuation of inventories, determined that the return did not reflect true income and instead of levying the tax upon the cash basis rewrote the taxpayer's return and levied a tax on what the commissioner apprehended was income.

The Supreme Court said in Gould v. Gould, 245 U. S. 153:

"In the interpretation of statutes levying taxes it is the established rule not to extend their provisions, by implication, beyond the clear import of the language used, or to enlarge their operations so as to embrace matters not specifically pointed out. In case of doubt they are construed most strongly against the Government, and in favor of the citizen."

The same court said in United States v. Anderson, 269 U. S. 422, at 441:

"It should be noted that section 13 (d) makes no use of the words 'accrue' or 'accrual' but merely provides for a return upon the basis upon which the taxpayer's accounts are kept, if it reflects income—which is precisely the return insisted upon by the Government."

The same court at page 437 says:

164 "Treasury Decision 2433 which provides in part that under section 13 (d) it 'will be permissible for corporations which accrue on their books monthly or at other stated periods amounts sufficient to meet fixed annual or other charges to deduct from their gross income the amounts so accrued, provided such accruals approximate as nearly as possible the actual liabilities for which the accruals are made, and provided that in cases wherein deductions are made on the accrual basis as hereinbefore indicated, income from fixed and determinable sources accruing to the corporations must be returned, for the purpose of the tax, on the same basis.' It also provided in substance that when the taxpayer, following a consistent accounting practice, sets up reserves to meet liabilities, the 'amount of which or date of maturity' is not definitely determinable, such reserve may be deducted from gross income. The decisions also laid down a procedure for readjusting such reserves when the amount actually required for that purpose was definitely ascertained, and provided that if returns upon this basis of 'accrual or reserves' did not reflect true net income, the taxpayer would not be permitted to make its return on any other basis than that of 'actual receipts and disbursements.'

"We think that the statute was correctly interpreted by the commissioner and that his decision referred to was consistent with its purpose and intent."

In fine the statute imposes a tax upon the cash income received. Section 13 (d) grants permission to the taxpayer to make a return upon the basis of accrued income. The only power which the commissioner has to levy a tax is upon income and, as the Supreme Court points out, if the net income is not reflected by the return
165 made, then there is no other basis than that of actual receipts and disbursements upon which the tax may be levied.

The Government's position is that there is an estoppel which bars the present action. The books, however, of the plaintiff companies have been carefully examined and they do reflect its income for the years in question upon the basis of actual receipts and disbursements, the basis upon which Congress imposed a tax. It is certainly no fault of the companies that the commissioner rejected the return made upon the basis upon which their books were kept. The fact that the actual cash income was less than the income which the companies' books reflect is no reason why the companies should be barred from recovering the taxes which were levied upon a basis not authorized by law.

It seems useless to comment further than to say that the companies are given the option of making a return upon the basis upon which their accounts are kept, and that basis is subject to regulation by the commissioner. Such a statute does not impose a tax upon the basis upon which the commissioner shall direct the books to be kept. The option is with the taxpayer to make the return upon the basis upon which its accounts are kept. The commissioner may reject this basis and levy the tax upon actual receipts and disbursements. He cannot in part reject and in part confirm the taxpayer's method of bookkeeping. If he could the tax might very well be an arbitrary adjustment reflecting anything but income.

It is not necessary to consider whether under the 16th amendment the commissioner may determine incomes upon the accrual basis, since Congress did not give him this power under the act of 1917.

Judgment may be entered accordingly.

166 In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Defendant's request for findings of fact and conclusions

Filed June 11, 1927

The defendant, considering the facts hereinafter set forth to be proven, and deeming them material to the due presentation of its case in the findings of fact, requests the court to find the same as follows:

1. The plaintiff was, during the time involved in this suit, a
now it, a corporation duly organized and existing under the la
of the State of New Jersey, having its legal residence and its pri
cipal office at Jersey City in the State of New Jersey, and is e
gaged in the business of manufacturing and selling cans and oth
containers.

2. During the time involved in this suit and up to March, 192
William H. Edwards was the collector of internal revenue for t
second district of New York, was not in office as collector of intern
revenue at the time of the filing of this suit, and Frank K. Bowe
since March, 1921, has been, and now is, collector of internal reven
for said district.

167 3. The plaintiff, which had, and now has, its principal bu
ness office in the said second district for New York, was
1917 the owner of all of the capital stock of the Missouri Can Co
pany, the Detroit Can Company, the American Can Company
Massachusetts, the American Can Company of Utah, the Sanita
Can Company, the Chas. W. Shonk Company, the Union Can Co
pany, the Davenport Can Company, the Newton Manufacturi
Company, the Wade Machine Company, the Raleigh Manufactu
ing Company, and the Newbern Box Company. The plaintiff a
its subsidiary or affiliated corporations kept their accounts on t
accrual basis, and the returns for income taxes for the year 1916
the plaintiff and its affiliated or subsidiary corporations were ma
upon the accrual basis. The returns of each and all of said corpo
tions for the year 1917 were made upon the accrual basis, and so t
were the returns for the year 1918.

4. Up to January 31, 1917, all of the inventories of the plaint
and its affiliated or subsidiary corporations, including the inventori
of tin plate, were uniformly valued at cost and were so valued
the returns for income tax for the year 1916.

5. Prior to 1917 there had been little or no fluctuation in the c
of tin plate. In January, 1917, the market price of tin plate a
vanced sharply from $3.60 per box to $7.00 per box. The plaint
and its affiliated or subsidiary corporations caused a determinati
to be made of what was deemed a normal stock of tin plate for t
corporations' business, fixing the quantity at approximately 1,668,0
base boxes, and as a result of this the inventory of January 1, 19
which was the closing inventory on December 31, 1916, was revalu
by the American Can Company and its affiliated or subsidiary c
porations, including the plaintiff, at $7.00 per box, and the sum
$5,671,500 was charged to inventories on hand and credited to
"inventory constant" account on January 31, 1917, as of Jan

168 ary 1, 1917. This amount represented the difference betwe
the cost of tin plate as set down in the closing inventories
December 31, 1916, of the plaintiff and its affiliated and subsidia
corporations (namely, $3.60 per box) and the prevailing market pr
of tin plate on January 31, 1917 (that is, $7.00 per box).

6. During 1917 the plaintiff and its affiliated or subsidiary corporations kept their accounts upon the basis of accruing their receipts and disbursements, valuing the arbitrary quantity of tin plate as set up in their books as a normal supply and carried in their inventories at a constant figure, regardless of changes in the cost or market value of tin plate, and valuing the other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased.

7. The plaintiff and its affiliated or subsidiary corporations carried in their inventories large stocks of tin plate, the value of their stocks of tin plate being approximately one-half of the total value of all the materials carried in their inventories.

8. For the year 1917 the plaintiff and all its affiliated or subsidiary corporations made and filed with William H. Edwards, as collector of internal revenue for the second district of New York, their income and excess profits tax returns for 1917. These returns were made upon the basis of accruing receipts and disbursements, using the so-called "inventory constant" set up in their books in January, 1917, in valuing that part of their inventories consisting of tin plate and cost for all other materials. The amount of the net income of the plaintiff as so determined and returned was $16,927,404.35, and the amount of the consolidated net income of the plaintiff and its affiliated or subsidiary corporations as so determined was $17,994,400.46. On or about June 14, 1918, the plaintiff paid to William H. Edwards, as collector of internal revenue for the second district of New
169 York, the sum of 869,418.99 as and for income tax for 1917 payable in accordance with its return as filed. At the same time the plaintiff paid excess-profits tax on the consolidated net income of itself and its affiliated or subsidiary corporations as so determined amounting to $2,397,080.87, or a total tax paid by the plaintiff of $3,266,499.86. The total amount of excess-profits taxes for 1917 payable by the plaintiff and its affiliated corporations was allocated to and paid by the plaintiff as the parent corporation.

9. The plaintiff, in making its return for the year 1917, returned the value of its inventory as amounting to $19,549,731.63. This amount was arrived at by deducting the sum representing the so-called "inventory constant" set up on the books by the plaintiff from the amount shown by the books of the plaintiff as the value of its actual inventory based upon cost.

10. Thereafter, and before September 21, 1920, the Commissioner of Internal Revenue, through his representatives, examined the books and records of the plaintiff and its affiliated or subsidiary corporations and made certain adjustments, which resulted in an assessment of additional income and excess-profits taxes aggregating $1,953,480.79, of which the plaintiff paid to William H. Edwards, as collector of internal revenue for the second district of New York, on or

about November 22, 1919, the sum of $520,762.54, and on or abo
September 21, 1920, the sum of $1,432,718.25.

11. Thereafter the Commissioner of Internal Revenue, throug
his representatives, again examined the books and records of th
plaintiff and its affiliated or subsidiary corporations, and objected
the basis upon which they had valued their inventories of tin pla
and determined their net incomes for 1917. On or about March
1921, the Commissioner of Internal Revenue issued and mailed le
ters to the plaintiff and its affiliated or subsidiary corporations,
which he stated in substance that the basis on which they ha
170 valued their inventory of tin plate and determined their n
incomes for 1917 was not correct, and undertook to revalu
their inventories of tin plate based upon cost, and to redetermi
their net incomes for 1917, and made adjustments which had th
effect of increasing the net income of the plaintiff to $22,933,625.7
and additional income taxes for 1917 amounting to $3,383,481.46.

12. On or about December 14, 1922, the plaintiff filed a claim for r
fund of income and excess-profits taxes for 1917 amounting to $3,343
139.35, which was made up of amounts included in the taxes whi
the plaintiff paid on June 14, 1918, November 22, 1919, and Septe
ber 21, 1920. It was stated in said claim, among other things, th
the Commissioner of Internal Revenue had determined that th
basis upon which the taxpayer had kept its accounts and made i
returns for 1917 did not clearly reflect the net income and had ca
culated the net income on a different basis and assessed addition
taxes as a result thereof, and that if the basis on which the taxpay
had kept its accounts did not clearly reflect its net income, the tax
should be computed on the basis of actual receipts and disbursement

13. On or after January 26, 1924, the Commissioner of Intern
Revenue disallowed and rejected the claim for refund.

14. The books of the plaintiff show that during the calendar ye
1917 the plaintiff received in cash the sum of $116,786,504.27 an
during the same period disbursed in cash the sum of $104,031,618.2
In setting up and proving its figures of actual cash receipts and di
bursements the plaintiff has used neither opening nor closing inve
tories for the year 1917, nor has the plaintiff, in setting up its clai
on the basis of cash receipts and disbursements, undertaken to
adjust and reconcile the accrual items, including bills payable, tak
in its return for the year 1916. The above amounts show the gro
amount of cash received by the plaintiff in 1917, and t
171 expenditures included (1) the ordinary and necessary expen
paid in 1917 in the maintenance and operation of the busin
and properties, (2) the losses actually sustained and charged off
1917 and not compensated by insurance or otherwise subject to t
limitations contained in paragraph second of subdivision (a)
section 12 of the revenue act of 1916, (3) the interest on indebtedn
paid in 1917 (except on indebtedness incurred for the purchase

obligations or securities, the interest upon which was exempt from taxation as income under said statute), subject to the limitations contained in paragraph third of subdivision (a) of section 12 of the revenue act of 1916, and (4) the taxes paid in 1917 imposed by the Government of the United States (except income and excess-profits taxes) or of its Territories or possessions or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits. The plaintiff has not shown the cost of manufacturing goods sold or the amount expended for the purchase of raw materials.

15. The Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, made regulations which provided that all materials carried in inventories should be valued on the basis of (a) cost or (b) cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased, and the basis upon which the plaintiff and its said affiliated companies kept their accounts and made their returns for 1917 was not in accordance with said regulations.

Conclusion of law

It is requested that the court adopt the following conclusion of law:

172 Upon the finding of fact herein the plaintiff is not entitled to recover, and the petition is hereby dismissed with costs.

The COURT. Requests denied.

Mr. HENDLER. Exception.

Exception allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

WALTER G. WINNE,
United States Attorney,
By JAS. S. TURP,
Assistant U. S. Attorney.
CHAS. T. HENDLER,
Special Attorney, Internal Revenue.
Attorneys for Defendant.

173 In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Motion for judgment for defendant

Comes now the defendant and moves the court that judgment be given for the defendant, because

(1) The plaintiff has failed to sustain the burden imposed upon it to prove that all or part of the taxes sought to be recovered back in this proceeding were wrongfully or unlawfully collected;

(2) There is not sufficient evidence to support a judgment against the defendant.

The COURT. Motion denied.

Mr. HENDLER. Exception.

Exception allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

WALTER G. WINNE,
United States Attorney,
By JAS. S. TURP,
Assistant U. S. Attorney.
CHAS. T. HENDLER,
Special Attorney, Internal Revenue.
Attorneys for Defendant.

174 In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Findings of fact and conclusions of law

Filed August 16, 1927

Findings of fact

The court finds that all the facts admitted by the pleadings are true, and also finds the following additional facts:

1. The plaintiff and its domestic affiliated corporations, to wit: the Missouri Can Company, the Detroit Can Company, the American Can Co. of Massachusetts, the American Can Company of Utah, the Sanitary Can Company, the Chas. W. Shonk Co., the Union Can Company, the Davenport Can Company, the Newton Manufacturing Co., the Wade Machine Company, the Raleigh Manufacturing Co., and the Newbern Box Company, corporations organized in the United States of which the plaintiff owned all, or substantially all, the stock, kept their accounts during 1917 upon the basis of accruing their receipts and disbursements, valuing the normal stocks of tin plate car-
175 ried in their inventories at a constant figure, regardless of changes in the cost or market value of tin plate, and valuing all other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased. The corporations above named were the only corporations organized in the United States

of which the plaintiff owned or controlled all, or substantially all, the stock in or during 1917, and there were no interests which owned or controlled substantially all the stock of the plaintiff and any other corporation in or during 1917.

2. The plaintiff and its domestic affiliated corporations determined their incomes and made their Federal income and excess profits tax returns for 1917 upon the basis upon which their accounts were kept. Said returns were filed in March, 1918, with William H. Edwards, the collector of internal revenue of the United States for the second district of New York. The amount of the net income of the plaintiff as so determined and returned was $16,927,404.35 (including $60,010.50 as dividends upon the stock of other domestic corporations) and the amount of the consolidated net income of the plaintiff and its domestic affiliated corporations as so determined and returned was $17,994,400.46 (including $60,010.50 as dividends upon the stock of other domestic corporations).

3. On or about June 14, 1918, the plaintiff paid, and William H. Edwards, as collector of internal revenue of the United States collected from the plaintiff, $3,266,499.86 as and for the income tax for 1917 payable by the plaintiff and the excess profits tax for 1917 payable by the plaintiff and its domestic affiliated corporations, in accordance with their returns as filed. The total amount of said excess profits tax was allocated to and paid by the plaintiff as the parent corporation.

4. After June 14, 1918, and prior to September 21, 1920,
176 the Commissioner of Internal Revenue made assessments against the plaintiff for additional income and excess profits taxes for 1917 aggregating $1,953,480.79. The plaintiff paid, and William H. Edwards, as collector of internal revenue of the United States, collected from the plaintiff, $520,762.54 on or about November 22, 1919, and $1,432,718.25 on or about September 21, 1920, as and for such additional taxes.

5. The Commissioner of Internal Revenue ruled and determined that the basis upon which the plaintiff and its domestic affiliated corporations kept their accounts and made their Federal income and excess profits tax returns for 1917 did not clearly reflect their incomes, that their incomes for 1917 should not be determined upon such basis and that their income and excess profits taxes for 1917 should not be computed upon their incomes as returned.

6. The gross amount of the income of the plaintiff received within the year 1917 from all sources was $116,786,504.27 (including $60,010.50 as dividends upon the stock of other domestic corporations). The amount of the ordinary and necessary expenses paid by the plaintiff within the year 1917 in the maintenance and operation of its business and properties, was $101,310,074.96. The amount of the losses actually sustained and charged off by the plaintiff within the year 1917 and not compensated by insurance or otherwise, was $1,641,325.01. The amount of the interest paid by the plaintiff

within the year 1917 on its indebtedness (not including any indebtedness incurred for the purchase of obligations or securities, the interest upon which was exempt from the Federal income tax) to an amount of such indebtedness not in excess of the amount of the paid-up capital stock of the plaintiff outstanding at the close of the year 1917, was $744,340.27. The amount of the taxes paid by the plaintiff within the year 1917 imposed by the authority of the United States (except income and excess profits taxes), or of its Territories or possessions, or any foreign country, or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits, was $335,878.01. The amount of the net income of the plaintiff for the year 1917, determined upon the basis of actual receipts and disbursements by deducting from the gross amount of its income received within the year from all sources all such expenses, interest and taxes paid within the year and all such losses actually sustained and charged off within the year was $12,754,886.02 (including $60,010.50 as dividends upon the stock of other domestic corporations). The amounts above mentioned for expenses, losses, interest and taxes include only expenses, losses, interest and taxes which are described in section 12 (a) of Title I of the act of Congress entitled, "An act to increase the revenue and for other purposes," approved September 8, 1916, as amended by the act of Congress entitled, "An act to provide revenue to defray war expenses and for other purposes," approved October 3, 1917, subject to the limitations and provisos therein mentioned.

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7. The gross amount of the income of each of the plaintiff's domestic affiliated corporations received within the year 1917 from all sources, the amount of the ordinary and necessary expenses paid by each of said corporations within the year 1917 in the maintenance and operation of its business and properties, the amount of the losses actually sustained and charged off by each of said corporations within the year 1917 and not compensated by insurance or otherwise, the amount of the interest paid by each of said corporations within the year 1917 on its indebtedness (not including any indebtedness incurred for the purchase of obligations or securities, the interest upon which was exempt from the Federal income tax) to an amount of such indebtedness not in excess of the amount of the paid-up capital stock of such corporation outstanding at the close of the year 1917, the amount of the taxes paid by each of said corporations within the year 1917 imposed by the authority of the United States (except income and excess profits taxes), or of its Territories or possessions, or any foreign country, or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits, and the amount of the net income of each of said corporations for the year 1917 determined upon the basis of actual receipts and disbursements by deducting from the gross

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amount of the income received within the year from all sources all such expenses, interest and taxes paid within the year and all such losses actually sustained and charged off within the year were as stated in Exhibit P–7, which is hereby incorporated in and made a part of this paragraph. The amounts given in said Exhibit P–7 for expenses, losses, interest and taxes include only expenses, losses, interest and taxes which are described in section 12 (a) of Title I of the act of Congress entitled, "An act to increase the revenue and for other purposes," approved September 8, 1916, as amended by the act of Congress entitled, "An act to provide revenue to defray war expenses and for other purposes," approved October 3, 1917, subject to the limitations and provisos therein mentioned. The Newbern Box Company received no gross or net income within the year 1917.

8. The gross amount of the incomes of the plaintiff and its domestic affiliated corporations received within the year 1917 from all sources was $125,938,490.78 (including $60,010.50 as dividends upon the stock of other domestic corporations). The amount of the ordinary and necessary expenses paid by the plaintiff and its domestic affiliated corporations within the year 1917 in the maintenance and operation of their business and properties was $109,733,841.28. The amount of the losses actually sustained and charged off by the plaintiff and its domestic affiliated corporations within the year
179 1917 and not compensated by insurance or otherwise, was $1,852,548.29. The amount of the interest paid by the plaintiff within the year 1917 on its indebtedness (not including any indebtedness incurred for the purchase of obligations or securities, the interest upon which was exempt from the Federal income tax) to an amount of such indebtedness not in excess of the amount of the paid-up capital stock of the plaintiff outstanding at the close of the year 1917, was $744,340.27. The amount of the interest paid by the domestic affiliated corporations of the plaintiff within the year 1917 on their indebtedness was nothing. The amount of the taxes paid by the plaintiff and its domestic affiliated corporations within the year 1917 imposed by the authority of the United States (except income and excess profits taxes) or of its Territories or possessions, or any foreign country, or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits, was $376,706.42. The amount of the consolidated net income of the plaintiff and its domestic affiliated corporations for the year 1917 determined upon the basis of actual receipts and disbursements by deducting from the gross amount of their incomes received within the year from all sources all such expenses, interest and taxes paid within the year, and all such losses actually sustained and charged off within the year, was $13,231,054.52 (including $60,010.50 as dividends upon the stock of other domestic corporations). The amounts above mentioned for expenses, losses, interest and taxes include only expenses, losses, interest and taxes which are described in section 12 (a) of Title I of the act

of Congress entitled, "An act to increase the revenue and for other purposes," approved September 8, 1916, as amended by the act of Congress entitled "An act to provide revenue to defray war expenses and for other purposes," approved October 3, 1917, subject to the limitations and provisos therein mentioned.

180 9. The net income of the plaintiff for 1917 ascertained upon the basis and in the manner provided in section 12 (a) of Title I of the act of Congress entitled, "An act to increase the revenue, and for other purposes," approved September 8, 1916, as amended by the act of Congress entitled, "An act to provide revenue to defray war expenses, and for other purposes," approved October 3, 1917, was $12,754,886.02 ($60,010.50 thereof being dividends upon the stock of other domestic corporations), and the consolidated net income of the plaintiff and its domestic affiliated corporations for 1917 ascertained upon the basis and in the manner provided in said section 12 (a) as so amended, was $13,231,054.52 ($60,010.50 being dividends upon the stock of other domestic corporations).

10. For the purpose of computing the Federal excess profits tax for 1917 payable by the plaintiff and its domestic affiliated corporations, the amount of the consolidated invested capital was $60,348,919.50 and the amount of the deduction from income was 9% of the consolidated invested capital plus $3,000 or $5,434,402.76.

11. The total amount of the Federal income taxes for 1917 payable by the plaintiff upon $12,754,886.02 of net income ($60,010.50 thereof being dividends upon the stock of other domestic corporations) and of the Federal excess profits tax for 1917 payable by the plaintiff and its domestic affiliated corporations upon $13,231,054.52 of consolidated net income ($60,010.50 thereof being dividends upon the stock of other domestic corporations) was $2,514,478.94.

12. No part of the amounts which the plaintiff has paid, or which William H. Edwards, as collector of internal revenue of the United States has collected from the plaintiff, as or for income or excess profits taxes for 1917, has been refunded or repaid to the plaintiff or credited against any income, war profits or excess profits

181 tax or installment thereof due from or payable by the plaintiff.

Conclusions of law

From the foregoing the court concludes:

1. The plaintiff has paid, and William H. Edwards, as collector of internal revenue of the United States, has collected from the plaintiff, as and for Federal income and excess profits taxes for 1917, $2,705,501.71 in excess of the amount which was legally payable and collectible, $752,020.92 thereof on or about June 14, 1918, $520,762.54 thereof on or about November 22, 1919, and $1,432,718.25 thereof on or about September 21, 1920. Said amounts were assessed and collected erroneously, illegally, wrongfully and without authority.

2. The plaintiff is entitled to judgment against the defendant for $2,705,501.71, with interest at the rate of 6% per annum on $752,020.92 from June 14, 1918, on $520,762.54 from November 22, 1919, and on $1,432,718.25 from September 21, 1920.

Let judgment be entered accordingly.

Dated, August 16, 1927.

J. L. BODINE, *District Judge.*

Mr. HENDLER. Exception to each of foregoing findings of fact and conclusions of law.

Exceptions allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

182 In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Judgment

Filed August 16, 1927

The above-entitled cause having duly come on to be heard before the above-entitled court, Honorable Joseph L. Bodine, judge thereof, presiding, and all parties having been present and represented by counsel and the cause having been heard and thereafter the court having caused a written opinion to be filed in the cause setting forth the specific findings by the court of the facts therein and the conclusions of the court upon all questions of law involved in the case, and having rendered judgment thereon,

Now, therefore, by virtue of the law and by reason of the premises aforesaid,

It is considered and adjudged that the plaintiff herein do have and recover of and from the defendant, the sum of $3,953,892.39, being the sum of $2,705,501.71, with interest at the rate of six per centum (6%) per annum on $752,020.92 from June 14, 1918, on
183 $520,762.54 from November 22, 1919, and on $1,432,718.25 from September 21, 1920.

Dated August 16, 1927.

J. L. BODINE, *Judge.*

Mr. HENDLER. Exception.

Exception allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Order extending term

Filed Sept. 17, 1927

This matter being opened to the court by Walter G. Winne, United States attorney for the District of New Jersey (by James S. Turp, assistant United States attorney):

It is on this 12th day of September, A. D. 1927, ordered that the April term of this court be and the same hereby is extended for a period of thirty days for the purpose of settling and signing bill of exceptions herein.

Entered Sept. 17, 1927. J. L. BODINE, *Judge.*

184 In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Order extending term

Filed Oct. 11, 1927

This matter being opened to the court by Walter G. Winne, United States attorney for the District of New Jersey (by James S. Turp, assistant United State attorney), and good cause being shown therefore:

It is on this 11th day of October, 1927, ordered that the April term of this court be and the same hereby is extended for an additional period of thirty days from October 12, 1927, for the purpose of settling and signing bill of exceptions herein.

J. L. BODINE, *Judge.*

185 In United States District Court

THE UNITED STATES, PLAINTIFF IN ERROR (DEFENDANT BELOW)

vs.

AMERICAN CAN COMPANY, DEFENDANT IN ERROR (PLAINTIFF BELOW)

Petition for writ of error

Filed Nov. 9, 1927

To the Honorable Judges of the United States District Court for the District of New Jersey:

And now comes the United States, defendant in the above entitled cause, by Walter G. Winne, United States attorney for the District

of New Jersey, and says that on the 16th day of August, 1927, the court entered judgment herein against defendant, for the sum of three million nine hundred fifty-three thousand eight hundred ninety-two dollars and thirty-nine cents ($3,953,892.39), in which final judgment and the proceedings had prior thereto in this cause, certain errors were committed to the prejudice of this defendant, all of which will more fully appear in the assignments of error filed with this petition.

Wherefore, this defendant prays that a writ of error may issue in this behalf to the United States Circuit Court of Appeals for the Third Circuit for the correction of the error so complained of
186 and that a transcript of the record of the proceedings and papers in this cause, duly authenticated, may be sent to the said court.

WALTER G. WINNE,
United States Attorney.
By JAS. S. TURP,
Assistant U. S. Attorney,
Attorneys for Defendant, (Plaintiff in Error).

In United States District Court

THE UNITED STATES, PLAINTIFF IN ERROR (DEFENDANT BELOW)

vs.

AMERICAN CAN COMPANY, DEFENDANT IN ERROR (PLAINTIFF BELOW)

Assignment of errors

Filed Nov. 9, 1927

And the said United States, defendant and plaintiff in error, by Walter G. Winne, United States attorney for the District of New Jersey, comes and says that in the record of the proceedings and in the findings of the court in said cause by the said District Court of the United States for the District of New Jersey, there is manifest error in this, to wit:

1. That the court erred in admitting statement computed by the plaintiff and marked Exhibit P–7.
2. That the court erred in admitting statement computed by plaintiff and marked Exhibit P–8.
187 3. That the court erred in admitting statements computed by plaintiff and marked Exhibits P–9, and P–9a.
4. That the court erred in admitting statement computed by the plaintiff and marked "P–11."

5. That the court erred in excluding answer to question of th witness Mr. Green as to whether it would be possible to show th income of the American Can Company by wholly disregarding th opening inventory and deducting the inventory of the goods on han and in process at the close of 1917, assuming that all of the earning of the American Can Company had been invested in raw materi during the year 1917.

6. That the court erred in excluding answer to question of th witness Mr. Green as to whether the company having kept the book of account on the accrual basis and having made returns for the year 1916, 1917, and 1918 on the accrual basis, the so-called cash receipt and disbursements basis without taking into account the openin and closing inventories for the year 1917, would correctly reflect th income of the American Can Company during the year 1917.

7. That the court erred in excluding statements computed by th defendant and marked for identification "Exhibits D–2 and D–3.

8. That the court erred in denying the motion of defendant fo judgment.

9. That the court erred in each and every of his findings of fact an conclusions of law.

10. That the court erred in denying the requests for findings o fact and conclusions of law presented by defendant.

11. That the court erred in finding judgment for the plaintiff.

Dated at Trenton, New Jersey, this 9th day of November, 1927.

WALTER G. WINNE, *United States Attorney.*

188 In United States District Court

THE UNITED STATES, PLAINTIFF IN ERROR (DEFENDANT BELOW)

VS.

AMERICAN CAN COMPANY, DEFENDANT IN ERROR (PLAINTIFF BELOW)

Order allowing writ of error

Filed Nov. 9, 1927

This 9th day of November, 1927, came the defendant, the Unite States of America, by Walter G. Winne, United States attorney, an filed herein and presented to the court his petition praying for th allowance of a writ of error intended to be urged by him; prayin also that the transcript of record and proceedings and papers, upo which the judgment herein was rendered, duly authenticated, may b sent to the United States Circuit Court of Appeals for the Thir Circuit, and that such other and further proceedings may be had may be proper in the premises.

On consideration whereof the court has allowed the writ or erro

J. L. BODINE, *Judge.*

189 United States Circuit Court of Appeals for the Third Circuit

Writ of error

Filed Nov. 9, 1927

THE UNITED STATES OF AMERICA,
Third Judicial Circuit, ss:

The President of the United States to the honorable Judges of the District Court of the United States for the District of New Jersey, greeting:

Because in the record and proceedings, as also in the rendition of the judgment, of a plea which in the said District Court, before you, or some of you, between American Can Company, plaintiff, and the United States, defendant, a manifest error hath happened, to the great damage of the said United States, defendant, as by his complaint appears, we being willing that error, if any hath been, should be duly corrected, and full and speedy justice done to the parties aforesaid in this behalf, do command you, if judgment be therein given, that then under your seal, distinctly and openly you send the record and proceedings aforesaid, with all things concerning the same, to the United States Circuit Court of Appeals for the Third Circuit, together with this writ, in said circuit on the 8th day of December next, so that you have the same at Philadelphia, in said circuit, on the 8th day of December next, in the said Circuit Court of Appeals, to be then and there held, that the record and proceedings aforesaid being inspected, the said Circuit Court of Appeals may cause further to be done therein to correct that error, what of right and according to laws and customs of the United States, should be done.

190 Witness, the Honorable William Howard Taft, Chief Justice of the United States, this 9th day of November, A. D. 1927.

[SEAL.] GEORGE T. CRANMER.

Attest:

_____ _____,
Clerk of the United States District Court,
District of New Jersey.
By CHARLES S. CHEVRIER,
Deputy.

[Citation in usual form showing service on John J. Treacy filed Nov. 15, 1927, omitted in printing.]

190A In United States District Court

AMERICAN CAN COMPANY, PLAINTIFF
vs.
THE UNITED STATES, DEFENDANT
} In Equity

Stipulation as to record

It is hereby stipulated and agreed, that the foregoing is a tru transcript of the record of the said District Court in the abov entitled matter as agreed on by the parties for the purposes of th appeal.

Dated Oct. 18th, 1928.

JOHN J. TREACY,
Attorney for Plaintiff.
JAMES W. MCCARTHY,
United States Attorney, Attorney for Defendant.

190B [Clerk's certificate to foregoing transcript omitted i printing.]

191 In United States District Court, District of New Jersey

MISSOURI CAN COMPANY, PLAINTIFF
vs.
THE UNITED STATES, DEFENDANT

Docket entries

Jan. 22, 1926. Petition filed.
Jan. 22, 1926. Affidavit of service filed.
Apr. 28, 1926. Answer filed.
Aug. 2, 1926. Notice of trial filed.
Sept. 4, 1926. Notice of trial filed.
Jan. 13, 1927. Trial. Adjourned to day to be fixed.
May 16, 1927. Trial. Adjourned to May 24, 1927.
May 24, 1927. Trial. Decision reserved.
May 31, 1927. Memorandum filed (see case 1772).
192 June 11, 1927. Defendant's request for findings of fact file
June 11, 1927. Motion for judgment for defendant filed.
Aug. 16, 1927. Findings of fact and conclusions of law filed.
Aug. 16, 1927. Rule for judgment final for plaintiff for $12,033.
and filed.
Sept. 17, 1927. Order extending term filed.
Oct. 11, 1927. Order extending term filed.
Nov. 9, 1927. Bill of exceptions filed (see E–1772).
Nov. 9, 1927. Assignment of errors filed.
Nov. 9, 1927. Petition for writ of error filed.

Nov. 9, 1927. Order allowing writ of error filed.
Nov. 9, 1927. Writ of error issued.
Nov. 9, 1927. Citation issued.
Nov. 15, 1927. Citation returned, service acknowledged. Copy filed.
Nov. 18, 1927. Order for leave to withdraw files for printing filed.

193 In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF

AGAINST

THE UNITED STATES, DEFENDANT

Petition

Filed Jan. 22, 1926

To the honorable Judges of the United States District Court for the District of New Jersey:

The petition of Missouri Can Company, the above named plaintiff, respectfully shows:

1. The plaintiff was during all the times hereinafter mentioned and now is a corporation duly organized and existing under the laws of the State of New Jersey, having its legal residence and its principal office in the State of New Jersey at Jersey City, Hudson County, in the District of New Jersey, and engaged in the business of manufacturing and selling cans and other containers.

2. On information and belief, that during all the times hereinafter mentioned up to March, 1921, one William H. Edwards was the collector of internal revenue of the United States for the second district of New York; that said Edwards is not now in office
194 as collector of internal revenue of the United States for said district and that one Frank K. Bowers, since March, 1921, has been and now is collector of internal revenue of the United States for said district.

3. The American Can Company, a corporation of New Jersey, which had, and now has its principal place of business in the said second district for New York, was in 1917 the owner of all of the capital stock of the plaintiff, the Detroit Can Company, the American Can Company of Massachusetts, the American Can Company of Utah, the Sanitary Can Company, the Chas. W. Shonk Company, the Union Can Company, the Davenport Can Company, the Newton Manufacturing Company, the Wade Machine Company, the Raleigh Manufacturing Company, and the Newburn Box Company, all of which companies are herein sometimes called "the plaintiff and its said affiliated companies." The plaintiff and its said affiliated companies kept their accounts during 1917 upon the basis of accruing

their receipts and disbursements, valuing the normal stocks of tin plate carried in their inventories at a constant figure regardless of changes in the cost or market value of tin plate and valuing the other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased. The plaintiff, the American Can Company, the Detroit Can Company, the American Can Company of Massachusetts, the American Can Company of Utah, and the Sanitary Can Company carried in their inventories large stocks of tin plate, and tin plate was the principal and by far the most important material used by the plaintiff and said companies in their business of manufacturing cans and other containers, the value of their stocks of tin plate being approximately one-half the total value of all the materials carried in their inventories. The plaintiff and all its said affiliated companies determined their incomes and duly made
195 and filed with said Edwards, as such collector of internal revenue, their income and excess profits tax returns for 1917 upon the basis upon which their accounts were kept. The amount of the net income of the plaintiff as so determined and returned was $253,559.18. On or about June 14, 1918, the plaintiff paid, and the said Edwards, as such collector of internal revenue, collected, from the plaintiff $15,213.54 as and for the income tax for 1917 payable by the plaintiff in accordance with said return. The total amount of the excess profits taxes for 1917, payable by the plaintiff and its said affiliated companies, was allocated to and paid by the American Can Company, as the parent company and collected by the said Edwards as such collector of internal revenue from the American Can Company.

4. Thereafter the Commissioner of Internal Revenue, through his representatives, examined the books and records of the plaintiff and its said affiliated companies and objected to the basis upon which the plaintiff and its said affiliated companies had valued their inventories of tin plate and determined their net incomes for 1917, and on or about March 7, 1921, the Commissioner of Internal Revenue issued and mailed letters to the plaintiff and American Can Company, in which he stated in substance that the basis on which the plaintiff had valued its inventory of tin plate and determined its net income for 1917 was not correct, and undertook to revalue its inventory of tin plate and to redetermine its net income for 1917 upon a different basis and made adjustments which had the effect of increasing the net income of the plaintiff to $422,059.18. On information and belief that thereafter the Commissioner of Internal Revenue, in accordance with said adjustments, made an asessment against the plaintiff for additional income taxes for 1917 amounting to $10,110.

5. On or about December 5, 1921, the plaintiff filed with said Bowers, as such collector of internal revenue, a claim for the
196 abatement of the full amount of said assessment amounting to $10,110, and on or about December 14, 1922, the plaintiff

duly made and filed with said Bowers, as such collector of internal revenue, according to the provisions of law in that regard and the regulations of the Secretary of the Treasury established in pursuance thereof, a claim for the refund of income and excess profits taxes for 1917 amounting to $6,214.12 (or such greater amount as was legally refundable) which were included in the taxes which the plaintiff had paid on June 14, 1918, as hereinbefore stated. Said claim for refund was made out in the form prescribed by said regulations, and all the facts relied upon in support of said claim were clearly set forth under oath. It was stated in said claim, among other things, that the Commissioner of Internal Revenue had determined that the basis upon which the taxpayer had kept its accounts and made its returns for 1917 did not clearly reflect the net income and had calculated the net income on a different basis and assessed additional taxes amounting to $10.110 as a result thereof; that if the basis on which the taxpayer had kept its accounts did not clearly reflect its net income, the taxes should be computed on the basis of actual receipts and disbursements; that the amount of the plaintiff's net income for 1917, calculated upon the basis of actual receipts and disbursements, was approximately $149,990.39; that the correct amount of the income taxes for 1917 payable by the plaintiff was not more than $8,999.42; that the excess profits tax return of the plaintiff for 1917 was consolidated with that of American Can Company and that the total excess profits tax for 1917 was allocated to and paid by that corporation; that the plaintiff had already paid as and for income taxes for 1917, $15,213.54; that the taxes so paid by the plaintiff were in excess of those properly collectible by at least $6,214.12, and that the amount of the excess should be refunded.

On information and belief that on or after January 26, 1924,
197 the Commissioner of Internal Revenue disallowed and rejected said claim for abatement and said claim for refund. Thereafter the plaintiff paid to said Bowers, as such collector of internal revenue, under protest, the amount of the assessment involved in said claim for abatement with interest, and duly brought an action against said Bowers in the District Court of the United States for the Southern District of New York to recover back the amount so paid. Said action is still pending undetermined.

6. The plaintiff has recently made a more careful and detailed calculation of its net income upon the basis of actual receipts and disbursements. On information and belief that the amount of the net income of the plaintiff for 1917, determined upon the basis of actual receipts and disbursements as defined in section 12–(a) of the revenue act of 1916, approved September 8, 1916, as amended by the revenue act of 1917, approved October 3, 1917, that is to say, by deducting from the gross amount of the income received in 1917 the amounts of (1) the ordinary and necessary expenses paid in 1917 in the maintenance and operation of the business and properties, (2) the losses actually sustained and charged off in 1917 and not

compensated by insurance or otherwise subject to the limitations contained in paragraph second of said section 12–(a), (3) the interest on indebtedness paid in 1917 (except on indebtedness incurred for the purchase of obligations or securities, the interest upon which was exempt from taxation as income under said act) subject to the limitations contained in paragraph third of said section 12–(a), and (4) the taxes paid in 1917 imposed by the Government of the United States (except income and excess-profits taxes) or of its Territories or possessions or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits, was not more than $123,997.66; that the correct amount of the in-
198 come taxes for 1917 payable by the plaintiff, in accordance with the revenue acts applicable thereto, was not more than $7,439.86, and that the plaintiff has paid, and the said Edwards, as such collector of internal revenue, has collected from the plaintiff at least $7,773.68 in excess of the amount properly due and payable.

7. On information and belief that the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, made regulations which provided that all materials carried in inventories should be valued on the basis of (a) cost or (b) cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased and that the basis upon which the plaintiff and its said affiliated companies kept their accounts and made their returns for 1917 was not in accordance with said regulations. On information and belief that the Commissioner of Internal Revenue ruled and determined that the basis upon which the plaintiff and its said affiliated companies valued their inventories of tin plate and determined their net incomes for 1917 did not clearly reflect their income and was not authorized or permitted by the revenue acts applicable to 1917 or the regulations made thereunder, that their incomes for 1917 should not be determined upon the basis upon which they kept their accounts and made their returns and their income and excess-profits taxes for 1917 should not be computed upon their incomes as returned. The plaintiff claims that the net incomes of the plaintiff and its said affiliated companies for 1917 should be determined upon the basis of actual receipts and disbursements as defined in section 12 (a) of the revenue act of 1916, as amended by the revenue act of 1917, and that their income and excess-profits taxes for 1917 should be computed upon their net incomes as so determined. There have been erroneously and illegally assessed against and collected from the plaintiff internal-revenue taxes, to wit: in-
199–200 come taxes for 1917 amounting to at least $7,773.68, and the plaintiff has paid to said Edwards, as such collector of internal revenue, as and for income taxes for 1917 the sum of at least

773.68, which was excessive and wrongfully collected. The said n of $7,773.68, with interest at the rate of six per centum (6%) annum from June 14, 1918, is the sum of money or other thing imed and the damages sought to be recovered by the plaintiff in s suit.

Wherefore the plaintiff prays judgment upon the facts and law l demands judgment against the defendant for the sum of 773.68, with interest at the rate of six per centum (6%) per annum m June 14, 1918, together with the costs of this suit.

JOHN J. TREACY,
Attorney for Plaintiff.

Office and post-office address, 1 Exchange Place, Jersey City, New sey.

Duly sworn to by Henry W. Phelps; jurat omitted in printing.]

In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF

AGAINST

THE UNITED STATES, DEFENDANT

Affidavit of service

Filed Jan. 22, 1926

TE OF NEW JERSEY,
County of Mercer, ss.

ohn J. Treacy, being duly sworn, deposes and says:

am the attorney for the plaintiff in the above-entitled suit. On 22d day of January, 1926, I filed the original petition in said with the clerk of the United States District Court for the District New Jersey, I served a copy of said petition upon the district rney of the United States for said district and I mailed a copy said petition, by registered letter, to the Attorney General for United States, all as provided in sections 5 and 6 of the act of gress, approved March 3, 1887, commonly known as the "Tucker "

JOHN J. TREACY.

ubscribed and sworn to before me this 22d day of January, 1926.

R. S. CHEVRIER, *Deputy Clerk.*

202 In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF
vs.
THE UNITED STATES, DEFENDANT
} On Petition, etc.

Answer

Filed April 28, 1926

Defendant, United States of America, appearing herein by Walter G. Winne, United States attorney for the District of New Jersey, says:

1. It admits the allegations contained in paragraphs 1, 2, 4, and 5 of the petition.

2. It has no knowledge or information sufficient to form a belief as to the allegations contained in paragraph 3 of the petition.

3. As to the allegations contained in paragraph 6 of the petition defendant has no knowledge or information as to the calculations made by plaintiff. It denies that any amount in excess of the amount properly due and payable was assessed and collected.

4. As to the allegations contained in paragraph 7 of the petition defendant admits the making of the regulations by the Commissioner of Internal Revenue and his rulings and determinations, but denies that the taxes assessed and collected were erroneous and illegal.

WALTER G. WINNE,
United States Attorney,
Attorney for Defendant.

203 Bill of exceptions

Printed on pages 30 and 74.

Memorandum

Printed on page 160.

In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF
vs.
THE UNITED STATES, DEFENDANT

Defendant's request for findings of fact and conclusions

Filed June 11, 1927

The defendant, considering the facts hereinafter set forth to be proven, and deeming them material to the due presentation of its

ee in the findings of fact, requests the court to find the same as llows:

1. The plaintiff was, during the time involved in this suit, 4 and now is, a corporation duly organized and existing under the laws of the State of New Jersey, having its legal residence d its principal office at Jersey City, in the State of New Jersey, d is engaged in the business of manufacturing and selling cans d other containers.

2. During the time involved in this suit and up to March, 1921, illiam H. Edwards was the collector of internal revenue for the cond district of New York, was not in office as collector of internal venue at the time of the filing of this suit, and Frank K. Bowers, nce March, 1921, has been, and now is, collector of internal revenue r said district.

3. The American Can Company, a corporation organized under e laws of New Jersey, which had, and now has, its principal place business in the said second district for New York, was in 1917 e owner of all of the capital stock of the plaintiff, the Detroit Can mpany, the American Can Company of Massachusetts, the Amer- n Can Company of Utah, the Sanitary Can Company, the Chas. . Shonk Company, the Union Can Company, the Davenport Can mpany, the Newton Manufacturing Company, the Wade Machine mpany, the Raleigh Manufacturing Company, and the Newbern x Company. The American Can Company and its subsidiary or liated corporations, including the plaintiff, kept their accounts the accrual basis, and the returns for income taxes for the year 16 by the American Can Company and its affiliated or subsidiary rporations, including the plaintiff, were made upon the accrual is. The returns of each and all of said corporations for the year 17 were made upon the accrual basis, and so, too, were the returns the year 1918.

4. Up to January 31, 1917, all of the inventories of the American n Company and its affiliated or subsidiary corporations, including inventories of tin plate, were uniformly valued at cost and were so valued in the returns for income tax for the year 1916.

5. Prior to 1917 there had been little or no fluctuation in the cost of tin plate. In January, 1917, the market price of tin te advanced sharply from $3.60 per box to $7.00 per box. The erican Can Company and its affiliated or subsidiary corporations sed a determination to be made of what was deemed a normal ck of tin plate for the corporations' business, fixing the quantity pproximately 1,668,000 base boxes, and as a result of this the in- tory of January 1, 1917, which was the closing inventory on ember 31, 1916, was revalued by the American Can Company its affiliated or subsidiary corporations, including the plaintiff, 7.00 per box, and the sum of $5,671,500 was charged to inven- es on hand and credited to an "Inventory constant" account on uary 31, 1917, as of January 1, 1917. This amount represented

the difference between the cost of tin plate as set down in the closing inventories of December 31, 1916, of the American Can Company and its affiliated and subsidiary corporations (namely, $3.60 per box) and the prevailing market price of tin plate on January 31, 1917 (that is, $7.00 per box).

6. During 1917 the American Can Company and its affiliated or subsidiary corporations, including the plaintiff, kept their accounts upon the basis of accruing their receipts and disbursements, valuing the arbitrary quantity of tin plate as set up in their books as a normal supply and carried in their inventories at a constant figure, regardless of changes in the cost or market value of tin plate, and valuing the other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased.

7. The American Can Company and its affiliated or subsidiary corporations carried in their inventories large stocks of tin plate, the value of their stocks of tin plate being approximately one-half of the total value of all the materials carried in their inventories.

206 8. For the year 1917 the American Can Company and all its affiliated or subsidiary corporations made and filed with William H. Edwards, as collector of internal revenue for the second district of New York, their income and excess-profits tax returns for 1917, and in making the returns used the so-called "inventory constant" set up in their books in January, 1917. The amount of the net income of the plaintiff as so determined and returned was $253,559.18. On or about June 14, 1918, the plaintiff paid to William H. Edwards, as collector of internal revenue for the second district of New York, the sum of $15.213.54 as and for income tax for 1917 payable in accordance with its return as filed. The total amount of excess-profits taxes for 1917 payable by the plaintiff and its affiliated corporations was allocated to and paid by the American Can Company as the parent corporation.

9. The plaintiff, in making its return for income taxes for the year 1917, returned its inventory as amounting to $877,474.71. This amount was arrived at by deducting the sum representing the so-called "inventory constant" set up on the books of the plaintiff from the amount shown by the books of the plaintiff as the value of its actual inventory based upon cost.

10. Thereafter the Commissioner of Internal Revenue, through his representatives, examined the books and records of the American Can Company and its affiliated or subsidiary corporations, including the plaintiff, and objected to the basis upon which they had valued their inventories of tin plate and determined their net incomes for 1917, and on or about March 7, 1921, the Commissioner of Internal Revenue issued and mailed letters to the plaintiff and American Can Company, in which he stated in substance that the basis on which the plaintiff had valued its inventory of tin plate and determined

its net income for 1917 was not correct, and undertook to revalue its inventory of tin plate based upon cost, and to redetermine its 207 net income for 1917, and made adjustments which had the effect of increasing the net income of the plaintiff to $422,059.18, and additional income taxes for 1917 amounting to $10,110.00.

11. On or about December 14, 1922, the plaintiff filed a claim for refund of income and excess-profits taxes for 1917 amounting to $6,214.12, which was included in the taxes which the plaintiff paid on June 14, 1918. It was stated in said claim, among other things, that the Commissioner of Internal Revenue had determined that the basis upon which the taxpayer had kept its accounts and made its returns for 1917 did not clearly reflect the net income and had calculated the net income on a different basis and assessed additional taxes as a result thereof, and that if the basis on which the taxpayer had kept its accounts did not clearly reflect its net income, the taxes should be computed on the basis of actual receipts and disbursements.

12. On or after January 26, 1924, the Commissioner of Internal Revenue disallowed and rejected the claim for refund.

13. The books of the plaintiff show that during the calendar year 1917 the plaintiff received in cash the sum of $1,005,779.96 and during the same period disbursed in cash the sum of $881,615.09. In setting up and proving its figures of actual cash receipts and disbursements the plaintiff has used neither opening nor closing inventories for the year 1917, nor has the plaintiff, in setting up its claim on the basis of cash receipts and disbursements, undertaken to readjust and reconcile the accrual items, including bills payable, taken in its return for the year 1916. The above amounts show the gross amount of cash received by the plaintiff in 1917, and the expenditures included (1) the ordinary and necessary expenses paid in 1917 in the maintenance and operation of the business and properties, (2) the losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise subject to the limitations contained 08 in paragraph second of subdivision (a) of section 12 of the revenue act of 1916, (3) the interest on indebtedness paid in 917 (except on indebtedness incurred for the purchase of obligations securities, the interest upon which was exempt from taxation as come under said statute), subject to the limitations contained in ragraph third of subdivision (a) of section 12 of the revenue act 1916, and (4) the taxes paid in 1917 imposed by the Government the United States (except income and excess-profits taxes) or its Territories or possessions or by the authority of any State, unty, school district, or municipality, or other taxing subdivision any State, not including those assessed against local benefits. The aintiff has not shown the cost of manufacturing goods sold or the nount expended for the purchase of raw materials.

14. The Commissioner of Internal Revenue, with the approval of e Secretary of the Treasury, made regulations which provided that

all materials carried in inventories should be valued on the basis of (a) cost or (b) cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased, and the basis upon which the plaintiff and its said affiliated companies kept their accounts and made their returns for 1917 was not in accordance with said regulations.

Conclusion of law

It is requested that the court adopt the following conclusion of law:

Upon the finding of facts herein the plaintiff is not entitled to recover, and the petition is hereby dismissed with costs.

The COURT. Requests denied.

209 Mr. HENDLER. Exception.

Exception allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]
WALTER G. WINNE,
United States Attorney,
By JAS. S. TURP,
Asst. U. S. Attorney,
CHAS. T. HENDLER,
Special Attorney, Internal Revenue,
Attorneys for Defendant.

210 In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDENT

Motion for judgment for defendant

Filed June 11, 1927.

Comes now the defendant and moves the court that judgment be given for the defendant, because—

(1) The plaintiff has failed to sustain the burden imposed upon it to prove that all or part of the taxes sought to be recovered back in this proceeding were wrongfull yor unlawfully collected.

(2) There is not sufficient evidence to support a judgment against the defendant.

The COURT. Motion denied.

Mr. HENDLER. Exception.

Exception allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

WALTER G. WINNE,
United States Attorney,
By JAS. S. TURP,
Assistant U. S. Attorney,
CHAS. T. HENDLER,
Special Attorney, Internal Revenue,
Attorneys for Defendant.

211 In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF

AGAINST

THE UNITED STATES, DEFENDANT

Findings of fact and conclusions

Filed August 16, 1927.

The court finds that all the facts admitted by the pleadings are true, and also finds the following additional facts:

1. The American Can Company, a corporation of New Jersey, which had and now has its principal place of business in the second district of New York, was in 1917 the owner of all the capital stock of the plaintiff, the American Can Company of Utah, the American Can Company of Massachusetts, the Detroit Can Company, the Sanitary Can Company, the Charles W. Shonk Company, the Union Can Company, the Davenport Can Company, the Newton Manufacturing Company, the Wade Machine Company, the Raleigh Manufacturing Company, and the Newbern Box Company, all of which companies were corporations organized in the United States and are herein sometimes called "the plaintiff and its said affiliated
212 companies." The plaintiff and its said affiliated companies kept their accounts during 1917 upon the basis of accruing their receipts and disbursements, valuing the normal stocks of tin plate carried in their inventories at a constant figure regardless of changes in the cost or market value of tin plate, and valuing the other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased.

2. The plaintiff and its said affiliated companies determined their incomes and made their Federal income and excess profit tax returns for 1917 upon the basis upon which their accounts were kept. Said

returns were filed in March, 1918, with William H. Edwards, the collector of internal revenue of the United States for the second district of New York. The amount of the net income of the plaintiff as so determined and returned was $253,559.18. On or about June 14, 1918, the plaintiff paid, and the said Edwards as such collector of internal revenue, collected from the plaintiff $15,213.54 as and for the income taxes for 1917 payable by the plaintiff in accordance with said return. The total amount of the excess profits tax for 1917 payable by the plaintiff and its said affiliated companies was allocated to and paid by the American Can Company as the parent corporation and was collected by the said Edwards as such collector of internal revenue from the American Can Company.

3. The Commissioner of Internal Revenue ruled and determined that the basis upon which the plaintiff and its said affiliated companies kept their accounts and made their Federal income and excess profits tax returns for 1917 did not clearly reflect their incomes, that their incomes for 1917 should not be determined upon such basis and that their income and excess profits taxes for 1917 should not be computed upon their incomes as returned.

4. The gross amount of the income of the plaintiff received within the year 1917 from all sources was $1,005,779.96. The amount
213 of the ordinary and necessary expenses paid by the plaintiff within the year 1917 in the maintenance and operation of its business and properties was $848,978.95. The amount of the losses actually sustained and charged off by the plaintiff within the year 1917 and not compensated by insurance or otherwise was $28,968.33. The amount of the taxes paid by the plaintiff within the year 1917 imposed by the authority of the United States (except income and excess profits taxes) or of its Territories or possessions, or any foreign country, or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits, was $3,667.81. The amount of the net income of the plaintiff for the year 1917, determined upon the basis of actual receipts and disbursements by deducting from the gross amount of its income received within the year from all sources all such expenses and taxes paid within the year and all such losses actually sustained and charged off within the year, was $124,164.87. The amounts above mentioned for expenses, losses, and taxes, included only expenses, losses, and taxes which are described in section 12 (a) of Title I of the act of Congress entitled, "An act to increase the revenue and for other purposes," approved September 8, 1916, as amended by the act of Congress, entitled, "An act to provide revenue to defray war expenses and for other purposes," approved October 3, 1917, subject to the limitations and provisos therein mentioned. The amount of the net income of the plaintiff for the year 1917 ascertained upon the basis and in the manner provided in said section 12 (a) as so amended, was $124,164.87.

5. The total amount of the Federal income taxes for 1917 payable by the plaintiff upon $124,164.87 of net income was $7,449.89. The American Can Company has paid to the defendant all Federal excess profits taxes for 1917 which have been assessed against or payable by the plaintiff or any of its said affiliated companies.

214 6. No part of the amount which the plaintiff has paid, or which William H. Edwards as collector of internal revenue of the United States has collected from the plaintiff as and for income taxes for 1917, has been refunded or repaid to the plaintiff or credited against any income, war profit or excess profits tax or instalment thereof due from or payable by the plaintiff.

Conclusions of law

From the foregoing the court concludes:

1. On or about June 14, 1918, the plaintiff paid, and William H. Edwards as collector of internal revenue of the United States, collected from the plaintiff as and for Federal income taxes for the year 1917, $7,763.65 in excess of the amount which was legally payable and collectible. Said amount was assessed and collected erroneously, illegally, wrongfully, and without authority.

2. The plaintiff is entitled to judgment against the defendant for $7,763.65 with interest at the rate of 6% per annum from June 14, 1918.

Let judgment be entered accordingly.

Dated: August 16, 1927.

J. L. BODINE, *District Judge.* [L. S.]

Mr. HENDLER. Exception to each of foregoing findings of fact and conclusions of law.

Exceptions allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

215 In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF

AGAINST

THE UNITED STATES, DEFENDANT

Judgment

Filed August 16, 1927

The above-entitled cause having duly come on to be heard before the above-entitled court, Honorable Joseph L. Bodine, judge thereof, presiding, and all parties having been present and represented by counsel and the cause having been heard and thereafter the court

having caused a written opinion to be filed in the cause setting fort the specific findings by the court of the facts therein and the con clusions of the court upon all questions of law involved in the cas and having rendered judgment thereon,

Now, therefore, by virtue of the law and by reason of the premise aforesaid,

It is considered and adjudged that the plaintiff herein do have an recover of and from the defendant the sum of $12,033.66, being th sum of $7,763.65 with interest at the rate of six per centum (6% per annum from June 14, 1918.

Dated, August 16, 1927.

J. L. BODINE, *Judge.* [L. S.]

216 Mr. HENDLER. Exception.

Exception allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Order extending term

Filed September 17, 1927

This matter being opened to the court by Walter G. Winne, Unite States attorney for the District of New Jersey (by James S. Tur assistant United States attorney):

It is on this 12th day of September, A. D. 1927, ordered that th April term of this court be and the same hereby is extended for period of thirty days for the purpose of settling and signing bill o exceptions herein.

J. L. BODINE, *Judge.* [L. S.]

Entered Sept. 17th, 1927.

217 In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Order extending term

Filed October 11, 1927

This matter being opened to the court by Walter G. Winne, Unite States attorney for the District of New Jersey (by James S. Tur

assistant United States attorney), and good cause being shown therefore:

It is on this 11th day of October, A. D. 1927, ordered that the April term of this court be, and the same hereby is, extended for an additional period of thirty days from October 12, 1927, for the purpose of settling and signing bill of exceptions herein.

J. L. BODINE, *Judge*. [L. S.]

218 In United States District Court

THE UNITED STATES, PLAINTIFF IN ERROR (DEFENDANT BELOW)

VS.

MISSOURI CAN COMPANY, DEFENDANT IN ERROR (PLAINTIFF BELOW)

Petition for writ of error

Filed Nov. 9, 1927

To the honorable judges of the United States District Court for the District of New Jersey:

And now comes the United States, defendant in the above-entitled cause, by Walter G. Winne, United States attorney for the District of New Jersey, and says that on the 16th day of August, 1927, the court entered judgment herein against defendant for the sum of twelve thousand thirty-three dollars and sixty-six cents ($12,033.66), in which final judgment and the proceedings had prior thereto in this cause, certain errors were committed to the prejudice of this
219 defendant, all of which will more fully appear in the assignment of error filed with this petition.

Wherefore this defendant prays that a writ of error may issue in this behalf to the United States Circuit Court of Appeals for the Third Circuit for the correction of the error so complained of and that a transcript of the record of the proceedings and papers in this cause, duly authenticated, may be sent to the said court.

WALTER G. WINNE,
United States Attorney.
By JAS. S. TURP,
Assistant U. S. Attorney,
Attorney for Defendant (Plaintiff in Error).

220 In United States District Court

THE UNITED STATES, PLAINTIFF IN ERROR (DEFENDANT BELOW)

VS.

MISSOURI CAN COMPANY, DEFENDANT IN ERROR (PLAINTIFF BELOW)

Assignment of errors

Filed Nov. 9, 1927

And the said United States, defendant and plaintiff in error, by Walter G. Winne, United States attorney for the District of New

Jersey, comes and says that in the record of the proceedings and in the findings of the court in said cause by the said District Court of the United States for the District of New Jersey, there is manifest error in this, to wit:

1. That the court erred in admitting statement computed by the plaintiff and marked "Exhibit P–7."

2. That the court erred in admitting statement computed by plaintiff and marked "Exhibit P–8."

3. That the court erred in admitting statements computed by plaintiff and marked "Exhibits P–9 and P–9a."

4. That the court erred in admitting statement computed by the plaintiff and marked "P–11."

221 5. That the court erred in excluding answer to question of the witness Mr. Green as to whether it would be possible to show the income of American Can Company by wholly disregarding the opening inventory and deducting the inventory of the goods on hand and in process at the close of 1917, assuming that all of the earnings of the American Can Company had been invested in raw material during the year 1917.

6. That the court erred in excluding answer to question of the witness Mr. Green as to whether the company having kept the books on account on the accrual basis and having made returns for the years 1916, 1917, and 1918 on the accrual basis, the so-called cash receipts and disbursements basis, without taking into account the opening and closing inventories for the year 1917, would correctly reflect the income of the American Can Company during the year 1917.

7. That the court erred in excluding statements computed by the defendant and marked for identification "Exhibits D–2 and D–3."

8. That the court erred in denying the motion of defendant for judgment.

9. That the court erred in each and every of his findings of fact and conclusions of law.

10. That the court erred in denying the requests for findings of fact and conclusions of law presented by defendant.

11. That the court erred in finding judgment for the plaintiff.

Dated at Trenton, New Jersey, this 9th day of November, 1927.

WALTER G. WINNE,
United States Attorney.

222 In United States District Court

THE UNITED STATES, PLAINTIFF IN ERROR
(DEFENDANT BELOW)

VS.

MISSOURI CAN COMPANY, DEFENDANT IN ERROR
(PLAINTIFF BELOW)

Order allowing writ of error

Filed Nov. 9, 1927

This 9th day of November, 1927, came the defendant, the United States of America, by Walter G. Winne, United States attorney, and filed herein and presented to the court his petition praying for the allowance of a writ of error intended to be urged by him; praying also that the transcript of record and proceedings and papers, upon which the judgment herein was rendered, duly authenticated, may be sent to the United States Circuit Court of Appeals for the Third Circuit, and that such other and further proceedings may be had as may be proper in the premises.

On consideration whereof the court has allowed the writ of error.

J. L. BODINE, *Judge.*

[L. S.]

223 United States Circuit Court of Appeals for the Third Circuit

Writ of error

Filed Nov. 9, 1927

THE UNITED STATES OF AMERICA,
Third Judicial Circuit, ss:

The President of the United States to the Honorable Judges of the District Court of the United States for the District of New Jersey, greeting:

Because in the record and proceedings, as also in the rendition of the judgment, of a plea which in the said District Court, before you, or some of you, between Missouri Can Company, plaintiff, and the United States, defendant, a manifest error hath happened, to the great damage of the said United States defendant, as by his complaint appears, we being willing that error, if any hath been, should be duly corrected and full and speedy justice done to the parties aforesaid in this behalf, do command you, if judgment be therein given, that then under your seal, distinctly and openly you send the record and proceedings aforesaid, with all things concerning the

same, to the United States Circuit Court of Appeals for the Third Circuit, together with this writ, in said circuit on the 8th day of December next, so that you have the same at Philadelphia, in said circuit on the 8th day of December next, in the said Circuit Court of Appeals, to be then and there held, that the record and pro-
224 ceedings aforesaid being inspected, the said Circuit Court of Appeals may cause further to be done therein to correct that error, what of right and according to laws and customs of the United States, should be done.

Witness, the Honorable William Howard Taft, Chief Justice of the United States, this 9th day of November, A. D. 1927.

[SEAL.] GEORGE T. CRANMER,

Attest: ——— ———,

Clerk of the United States District Court,
District of New Jersey.

By CHARLES S. CHEVRIER,
Deputy.

225 [Citation in usual form showing service on John J. Treacy, filed Nov. 15, 1927, omitted in printing.]

225–A In United States District Court

MISSOURI CAN COMPANY, PLAINTIFF
vs.
THE UNITED STATES, DEFENDANT
} In equity

Stipulation as to record

It is hereby stipulated and agreed, that the foregoing is a true transcript of the record of the said District Court in the above-entitled matter as agreed on by the parties for the purposes of this appeal.

Dated Oct. 18th, 1928.

JOHN J. TREACY,
Attorney for Plaintiff.
JAMES A. MCCARTHY,
United States Attorney,
Attorney for Defendant.

225–B [Clerk's certificate to foregoing transcript omitted in printing.]

226 In United States District Court, District of New Jersey

DETROIT CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Docket entries

Jan. 22, 1926. Petition filed.
Jan. 22, 1926. Affidavit of service filed.

Apr. 28, 1926. Answer filed.
Aug. 2, 1926. Notice of trial filed.
Sept. 4, 1926. Notice of trial filed.
Jan. 13, 1927. Trial adjourned to day to be fixed.
May 16, 1927. Trial. Adjourned to May 24, 1927.
May 24, 1927. Trial. Decision reserved.
May 31, 1927. Memorandum filed (see case 1772).
June 11, 1927. Defendant's request for findings of fact, filed.
June 11, 1927. Motion for judgment for defendant filed.
Aug. 16, 1927. Findings of fact and conclusions of law filed.
Aug. 16, 1927. Rule for judgment final for plaintiff for $9,135.39, d filed.
Sept. 17, 1927. Order extending term filed.
Oct. 11, 1927. Order extending term filed.
7 Nov. 9, 1927. Bill of exceptions filed (see Case E*-1772).
Nov. 9, 1927. Assignment of errors filed.
Nov. 9, 1927. Petition for writ of error filed.
Nov. 9, 1927. Order allowing writ of error filed.
Nov. 9, 1927. Writ of error issued.
Nov. 9, 1927. Citation issued.
Nov. 15, 1927. Citation returned, service acknowledged. Copy ed.
Nov. 18, 1927. Order for leave to withdraw files for printing filed.

In United States District Court

DETROIT CAN COMPANY, PLAINTIFF

AGAINST

THE UNITED STATES, DEFENDANT

Petition

Filed Jan. 22, 1926

the Honorable Judges of the United States District Court for the District of New Jersey:

The petition of Detroit Can Company, the above named plaintiff, pectfully shows:

1. The plaintiff was during all the times hereinafter men- 8 tioned up to January 9, 1919, a corporation duly organized and existing under the laws of the State of New Jersey en- ged in the business of manufacturing and selling cans and other ntainers. On January 9, 1919, the plaintiff, by proceedings duly d and taken, was dissolved, and since that date it has been and now a body corporate for the purpose of prosecuting and defending ts by or against it. The plaintiff, during all the times herein- er mentioned, had and now has its legal residence and its principal ce in the State of New Jersey at Jersey City, Hudson County, in District of New Jersey.

2. On information and belief, that during all the times hereinafter mentioned up to March, 1921, one William H. Edwards was the collector of internal revenue of the United States for the second district of New York; that said Edwards is not now in office as collector of internal revenue of the United States for said district and that one Frank K Bowers, since March, 1921, has been and now is collector of internal revenue of the United States for said district.

3. The American Can Company, a corporation of New Jersey, which had, and now has its principal place of business in the said second district for New York, was in 1917 the owner of all of the capital stock of the plaintiff, the American Can Company of Utah, the American Can Company of Massachusetts, the Missouri Can Company, the Sanitary Can Company, the Chas. W. Shonk Company, the Union Can Company, the Davenport Can Company, the Newton Manufacturing Company, the Wade Machine Company, the Raleigh Manufacturing Company, and the Newburn Box Company, all of which companies are herein sometimes called "the plaintiff and its said affiliated companies." The plaintiff and its said affiliated companies kept their accounts during 1917 upon the basis of accruing their receipts and disbursements, valuing the normal stocks
229 of tin plate carried in their inventories at a constant figure regardless of changes in the cost or market value of tin plate and valuing the other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased. The plaintiff, the American Can Company, the American Can Company of Utah, the American Can Company of Massachusetts, the Missouri Can Company, and the Sanitary Can Company carried in their inventories large stocks of tin plate, and tin plate was the principal and by far the most important material used by the plaintiff and said companies in their business of manufacturing cans and other containers, the value of their stocks of tin plate being approximately one-half the total value of all the materials carried in their inventories. The plaintiff and all its said affiliated companies determined their incomes and duly made and filed with said Edwards, as such collector of internal revenue, their income and excess profits tax returns for 1917 upon the basis upon which their accounts were kept. The amount of the net income of the plaintiff as so determined and returned was $104,786.64. On or about June 14, 1918, the plaintiff paid, and the said Edwards, as such collector of internal revenue, collected, from the plaintiff $6.287.19 as and for the income tax for 1917 payable by the plaintiff in accordance with said return. The total amount of the excess profits taxes for 1917, payable by the plaintiff and its said affiliated companies, was allocated to and paid by the American Can Company as the parent company and collected by the said Edwards as such collector of internal revenue from the American Can Company.

4. Thereafter the Commissioner of Internal Revenue, through his epresentatives, examined the books and records of the plaintiff and ts said affiliated companies and objected to the basis upon which the laintiff and its said affiliated companies had valued their inventories of tin plate and determined their net incomes for 1917, and on 30 or about March 7, 1921, the Commissioner of Internal Revenue issued and mailed letters to the plaintiff and American Can Company, in which he stated in substance that the basis on which the laintiff had valued its inventory of tin plate and determined its net ncome for 1917 was not correct, and undertook to revalue its inven- ory of tin plate and to redetermine its net income for 1917 upon a ifferent basis and made adjustments which had the effect of increas- ng the net income of the plaintiff to $174,786.64. On information nd belief that thereafter the Commissioner of Internal Revenue, in ccordance with said adjustments, made an assessment against the laintiff for additional income taxes for 1917 amounting to $4.200.

5. On or about December 5, 1921, the plaintiff filed with said owers, as such collector of internal revenue, a claim for the abate- ent of the full amount of said assessment amounting to $4.200, and n or about December 14, 1922, the plaintiff duly made and filed with id Bowers, as such collector of internal revenue, according to the rovisions of law in that regard and the regulations of the Secretary f the Treasury established in pursuance thereof, a claim for the efund of income and excess profits taxes for 1917 amounting to ,568.06 (or such greater amount as was legally refundable) which ere included in the taxes which the plaintiff had paid on June 14, 918, as hereinbefore stated. Said claim for refund was made out the form prescribed by said regulations, and all the facts relied pon in support of said claim were clearly set forth under oath. It as stated in said claim, among other things, that the Commissioner Internal Revenue had determined that the basis upon which the xpayer had kept its accounts and made its returns for 1917 did t clearly reflect the net income and had calculated the net income a different basis and assessed additional taxes amounting to $4,200 as a result thereof; that if the basis on which the taxpayer 1 had kept its accounts did not clearly reflect its net income, the taxes should be computed on the basis of actual receipts d disbursements; that the amount of the plaintiff's net income for 17, calculated upon the basis of actual receipts and disbursements, as approximately $61,985.49; that the correct amount of the in- me taxes for 1917 payable by the plaintiff was not more than ,719.13; that the excess profits tax return of the plaintiff for 1917 as consolidated with that of American Can Company and that the tal excess profits tax for 1917 was allocated to and paid by that rporation; that the plaintiff had already paid as and for income xes for 1917 $6,287.19; that the taxes so paid by the plaintiff were excess of those properly collectible by at least $2,568.06 and that

the amount of the excess should be refunded. On information and belief that on or after January 26, 1924, the Commissioner of Internal Revenue disallowed and rejected said claim for abatement and said claim for refund. Thereafter the plaintiff paid to said Bowers, as such collector of internal revenue, under protest, the amount of the assessment involved in said claim for abatement with interest, and duly brought an action against said Bowers in the District Court of the United States for the Southern District of New York to recover back the amount so paid. Said action is still pending undetermined.

6. The plaintiff has recently made a more careful and detailed calculation of its net income upon the basis of actual receipts and disbursements. On information and belief that the amount of the net income of the plaintiff for 1917, determined upon the basis of actual receipts and disbursements as defined in section 12 (a) of the revenue act of 1916, approved September 8, 1916, as amended by the revenue act of 1917, approved October 3, 1917, that is to say, by deducting from the gross amount of the income received in 1917 the amounts of (1) the ordinary and necessary expenses paid in
232 1917 in the maintenance and operation of the business and properties, (2) the losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise subject to the limitations contained in paragraph second of said section 12 (a), (3) the interest on indebtedness paid in 1917 (except on indebtedness incurred for the purchase of obligations or securities, the interest upon which was exempt from taxation as income under said act) subject to the limitations contained in paragraph third of said section 12 (a), and (4) the taxes paid in 1917 imposed by the Government of the United States (except income and excess profits taxes) or of its Territories or possessions or by the authority of any State, county, school district, or municipality or other taxing subdivision of any State, not including those assessed against local benefits, was not more than $6,554.14; that the correct amount of the income taxes for 1917 payable by the plaintiff, in accordance with the revenue acts applicable thereto, was not more than $393.25, and that the plaintiff has paid, and the said Edwards, as such collector of internal revenue has collected, from the plaintiff at least $5,893.94 in excess of the amount properly due and payable.

7. On information and belief, that the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, made regulations which provided that all materials carried in inventories should be valued on the basis of (a) cost or (b) cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased and that the basis upon which the plaintiff and its said affiliated companies kept their accounts and made their returns for 1917 was not in accordance with said regulations. On information and belief that the Commissioner

f Internal Revenue ruled and determined that the basis upon which the plaintiff and its said affiliated companies valued their in-
3 ventories of tin plate and determined their net incomes for 1917 did not clearly reflect their incomes and was not authorized r permitted by the revenue acts applicable to 1917 or the regulations ade thereunder, that their incomes for 1917 should not be deter-ined upon the basis upon which they kept their accounts and made eir returns and their income and excess profits taxes for 1917 ould not be computed upon their incomes as returned. The plain-ff claims that the net incomes of the plaintiff and its said affiliated mpanies for 1917 should be determined upon the basis of actual ceipts and disbursements as defined in section 12 (a) of the revenue t of 1916, as amended by the revenue act of 1917, and that their come and excess profits taxes for 1917 should be computed upon eir net incomes as so determined. There have been erroneously nd illegally assessed against and collected from the plaintiff internal evenue taxes, to wit: income taxes for 1917 amounting to at least 5,893.94, and the plaintiff has paid to said Edwards, as such collector f internal revenue, as and for income taxes for 1917 the sum of at ast $5,983.94, which was excessive and wrongfully collected. The id sum of $5,893.94 with interest at the rate of six per centum (6%) er annum from June 14, 1918, is the sum of money or other thing aimed and the damages sought to be recovered by the plaintiff in is suit.

Wherefore the plaintiff prays judgment upon the facts and law and emands judgment against the defendant for the sum of $5,893.94, ith interest at the rate of six per centum (6%) per annum from ne 14, 1918, together with the costs of this suit.

JOHN J. TREACY, Esq.,
Attorney for Plaintiff.

Office and post-office address, 1 Exchange Place, Jersey City, New rsey.

4-235 [*Duly sworn to by Rensselaer H. Ismon, jurat omitted in printing.*]

6 In United States District Court

DETROIT CAN COMPANY, PLAINTIFF

AGAINST

THE UNITED STATES, DEFENDANT

Affidavit of Service

Filed Jan. 22, 1926

ATE OF NEW JERSEY,
County of Mercer, ss:

JOHN J. TREACY, being duly sworn, deposes and says:
I am the attorney for the plaintiff in the above-entitled suit. On e 22d day of January, 1926, I filed the original petition in said

suit with the clerk of the United States District Court for the District of New Jersey, I served a copy of said petition upon the district attorney of the United States for said district and I mailed a copy of said petition, by registered letter, to the Attorney General for the United States, all as provided in sections 5 and 6 of the act of Congress, approved March 3, 1887, commonly known as the "Tucker Act."

JOHN J. TREACY.

Subscribed and sworn to before me this 22d day of January, 1926.
R. S. CHEVRIER, *Deputy Clerk.*

237 In United States District Court

DETROIT CAN COMPANY, PLAINTIFF
vs.
THE UNITED STATES, DEFENDANT
} On Petition, etc.

Answer

Filed April 28, 1926

Defendant, United States of America, appearing herein by Walter G. Winne, United States Attorney for the District of New Jersey, answering, says:

1. It admits the allegations contained in paragraphs 1, 2, 4, and 5 of the petition.

2. It has no knowledge or information sufficient to form a belief as to the allegations contained in paragraph 3 of the petition.

3. As to the allegations contained in paragraph 6 of the petition defendant has no knowledge or information as to the calculations made by plaintiff. It denies that any amount in excess of the amount properly due and payable was assessed and collected.

4. As to the allegations contained in paragraph 7 of the petition defendant admits the making of the regulations by the Commissioner of Internal Revenue and his rulings and determinations, but denies that the taxes assessed and collected were erroneous and illegal.

WALTER G. WINNE,
United States Attorney,
Attorney for Defendant.

238 Bill of Exceptions

Printed on pages 30 and 74.

Memorandum

Printed on page 160.

In United States District Court

DETROIT CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Defendant's request for findings of fact and conclusions

Filed June 11, 1927

The defendant, considering the facts hereinafter set forth to be proven, and deeming them material to the due presentation of its case in the findings of fact, requests the court to find the same as follows:

1. The plaintiff was, during the time involved in this suit,
239 and up to January 9, 1919, a corporation duly organized and existing under the laws of the State of New Jersey, having its legal residence and its principal office at Jersey City, in the State of New Jersey, and engaged in the business of manufacturing and selling cans and other containers. On January 9, 1919, the plaintiff, by proceedings duly had and taken, was dissolved, and since that date it has been and now is a body corporate for the purpose of presenting or defending suits by or against it.

2. During the time involved in this suit and up to March, 1921, William H. Edwards was the collector of internal revenue for the second district of New York, was not in office as collector of internal revenue at the time of the filing of this suit, and Frank K. Bowers, since March, 1921, has been, and now is, collector of internal revenue for said district.

3. The American Can Company, a corporation organized under the laws of New Jersey, which had, and now has, its principal place of business in the said second district for New York, was in 1917 the owner of all of the capital stock of the plaintiff, the Missouri Can Company, the American Can Company of Massachusetts, the American Can Company of Utah, the Sanitary Can Company, the Chas. W. Shonk Company, the Union Can Company, the Davenport Can Company, the Newton Manufacturing Company, the Wade Machine Company, the Raleigh Manufacturing Company, and the Newbern Box Company. The American Can Company and its subsidiary or affiliated corporations, including the plaintiff, kept their accounts on the accrual basis, and the returns for income taxes for the year 1916 by the American Can Company and its affiliated or subsidiary corporations, including the plaintiff, were made upon the accrual basis. The returns of each and all of said corporations for the year 1917 were made upon the accrual basis, and so too were the returns for the year 1918.

4. Up to January 31, 1917, all of the inventories of the
240 American Can Company and its affiliated or subsidiary cor-
porations, including the inventories of tin plate, were uni-
formly valued at cost and were so valued in the returns for income
tax for the year 1916.

5. Prior to 1917 there had been little or no fluctuation in the cost
of tin plate. In January, 1917, the market price of tin plate ad-
vanced sharply from $3.60 per box to $7.00 per box. The American
Can Company and its affiliated or subsidiary corporations caused a
determination to be made of what was deemed a normal stock of tin
plate for the corporations' business, fixing the quantity at approxi-
mately 1,668,000 base boxes, and as a result of this inventory of
January 1, 1917, which was the closing inventory on December 31,
1916, was revalued by the American Can Company and its affiliated
or subsidiary corporations, including the plaintiff, at $7.00 per box
and the sum of $5,671,500 was charged to inventories on hand and
credited to an "Inventory constant" account on January 31, 1917
as of January 1, 1917. This amount represented the difference be-
tween the cost of tin plate as set down in the closing inventories of
December 31, 1916, of the American Can Company and its affiliated
and subsidiary corporations (namely, $3.60 per box) and the pre-
vailing market price of tin plate on January 31, 1917 (that is, $7.00
per box).

6. During 1917 the American Can Company and its affiliated or
subsidiary corporations, including the plaintiff, kept their account
upon the basis of accruing their receipts and disbursements, valuing
the arbitrary quantity of tin plate as set up in their books as a normal
supply and carried in their inventories at a constant figure, regard-
less of changes in the cost or market value of tin plate, and valuing
the other materials carried in their inventories at cost or market
value, whichever was lower, with the presumption that the material
in the inventory were those last purchased.

7. The American Can Company and its affiliated or subsi-
241 diary corporations carried in their inventories large stocks of
tin plate, the value of their stocks of tin plate being approxi-
mately one-half of the total value of all the materials carried in their
inventories.

8. For the year 1917 the American Can Company and all its
affiliated or subsidiary corporations made and filed with William H.
Edwards, as collector of internal revenue for the second district of
New York, their income and excess-profits tax returns for 1917.
These returns were made upon the basis of accruing receipts and
disbursements, using the so-called "inventory constant" set up in
their books in January, 1917, in valuing that part of their inventories
consisting of tin plate and cost for all other materials. The amount
of the net income of the plaintiff as so determined and returned was

$104,386.64. On or about June 14, 1918, the plaintiff paid to William H. Edwards, as collector of internal revenue for the second district of New York the sum of $6,287.19 as and for income tax for 1917 payable in accordance with its return as filed. The total amount of excess-profits taxes for 1917 payable by the plaintiff and its affiliated corporation was allocated to and paid by the American Can Company as the parent corporation.

9. The plaintiff, in making its return for income taxes for the year 1917, returned the value of its inventory as amounting to $175,540.13. This amount was arrived at by deducting the sum representing the so-called "inventory constant" set up on the books of the plaintiff from the amount shown by the books of the plaintiff as the value of its actual inventory based upon cost.

10. Thereafter the Commissioner of Internal Revenue, through his representatives, examined the books and records of the American Can Company and its affiliated or subsidiary corporations, including the plaintiff, and objected to the basis upon which they had valued their inventories of tin plate and determined their net income for 1917. On or about March 7, 1921, the Commissioner of In-
242 ternal Revenue issued and mailed letters to the plaintiff and American Can Company, in which he stated in substance that the basis on which the plaintiff had valued its inventory of tin plate and determined its net income for 1917 was not correct, and undertook to revalue its inventory of tin plate based upon cost, and to redetermine its net income for 1917, and made other adjustments which had the effect of increasing the net income of the plaintiff to $174,786.64, and additional income taxes for 1917 amounting to $4,200.00.

11. On or about December 14, 1922, the plaintiff filed a claim for refund of income and excess profits taxes for 1917 amounting to $2,568.06, which was included in the taxes which the plaintiff paid on June 14, 1918. It was stated in said claim, among other things, that the Commissioner of Internal Revenue had determined that the basis upon which the taxpayer had kept its accounts and made its returns for 1917 did not clearly reflect the net income and had calculated the net income on a different basis and assessed additional taxes as a result thereof, and that if the basis on which the taxpayer had kept its accounts did not clearly reflect its net income, the taxes should be computed on the basis of actual receipts and disbursements.

12. On or after January 26, 1924, the Commissioner of Internal Revenue disallowed and rejected the claim for refund.

13. The books of the plaintiff show that during the calendar year 1917 the plaintiff received in cash the sum of $241,246.48 and during the same period disbursed in cash the sum of $234,690.00. In setting up and proving its figures of actual cash receipts and disbursements the plaintiff has used neither opening nor closing inventories for the year 1917, nor has the plaintiff, in setting up its claim on the basis of cash receipts and disbursements, undertaken to readjust and reconcile

the accrual items, including bills payable, taken in its return for the year 1916. The above amounts show the gross amount
243 of cash received by the plaintiff in 1917, and the expenditures included (1) the ordinary and necessary expenses paid in 1917 in the maintenance and operation of the business and properties; (2) the losses actually sustained and charged off in 1917 and not compensated by insurance or otherwise subject to the limitations contained in paragraph second of subdivision (a) of section 12 of the revenue act of 1916; (3) the interest on indebtedness paid in 1917 (except on indebtedness incurred for the purchase of obligations or securities, the interest upon which was exempt from taxation as income under said statute), subject to the limitations contained in paragraph third of subdivision (a) of section 12 of the revenue act of 1916; and (4) the taxes paid in 1917 imposed by the Government of the United States (except income and excess-profits taxes) or of its Territories or possessions or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits. The plaintiff has not shown the cost of manufacturing goods sold or the amount expended for the purchase of raw materials.

14. The Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, made regulations which provided that all materials carried in inventories should be valued on the basis of (a) cost or (b) cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased, and the basis upon which the plaintiff and its said affiliated companies kept their accounts and made their returns for 1917 was not in accordance with said regulations.

244 Conclusion of law

It is requested that the court adopt the following conclusion of law:

Upon the finding of facts herein the plaintiff is not entitled to recover, and the petition is hereby dismissed with costs.

The COURT. Requests denied.

Mr. HENDLER. Exception.

Exception allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

WALTER G. WINNE,
United States Attorney,
By JAS. S. TURP,
Asst. U. S. Attorney,
CHAS. T. HENDLER,
Special Attorney, Internal Revenue,
Attorneys for Defendant.

245 In United States District Court

DETROIT CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Motion for judgment for defendant

Filed June 11, 1927

Comes now the defendant and moves the court that judgment be given for the defendant, because

(1) The plaintiff has failed to sustain the burden imposed upon it to prove that all or part of the taxes sought to be recovered back in this proceeding were wrongfully or unlawfully collected;

(2) There is not sufficient evidence to support a judgment against the defendant.

The COURT. Motion denied.

Mr. HENDLER. Exception.

Exception allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

WALTER G. WINNE,
United States Attorney,
By JAS. S. TURP,
Assistant U. S. Attorney,
CHAS. T. HENDLER,
Special Attorney, Internal Revenue,
Attorneys for Defendant.

246 In United States District Court

DETROIT CAN COMPANY, PLAINTIFF

AGAINST

THE UNITED STATES, DEFENDANT

Findings of fact and conclusions

Filed August 16, 1927

The court finds that all the facts admitted by the pleadings are true, and also finds the following additional facts:

1. The American Can Company, a corporation of New Jersey, which had and now has its principal place of business in the second district of New York, was in 1917 the owner of all the capital stock of the plaintiff, the American Can Company of Utah, the American

Can Company of Massachusetts, the Missouri Can Company, the Sanitary Can Company, the Charles W. Shonk Company, the Union Can Company, the Davenport Can Company, the Newton Manufacturing Company, the Wade Machine Company, the Raleigh Manufacturing Company, and the Newbern Box Company, all of which companies were corporations organized in the United States and are herein sometimes called "the plaintiff and its said affiliated companies." The plaintiff and its said affiliated companies kept
247 their accounts during 1917 upon the basis of accruing their receipts and disbursements, valuing the normal stocks of tin plate carried in their inventories at a constant figure regardless of changes in the cost or market value of tin plate, and valuing the other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased.

2. The plaintiff and its said affiliated companies determined their incomes and made their Federal income and excess-profits tax returns for 1917 upon the basis upon which their accounts were kept. Said returns were filed in March, 1918, with William H. Edwards, the collector of internal revenue of the United States for the second district of New York. The amount of the net income of the plaintiff as so determined and returned was $104,786.64. On or about June 14, 1918, the plaintiff paid, and the said Edwards as such collector of internal revenue, collected from the plaintiff $6,287.19 as and for the income taxes for 1917 payable by the plaintiff in accordance with said return. The total amount of the excess-profits tax for 1917 payable by the plaintiff and its said affiliated companies was allocated to and paid by the American Can Company as the parent corporation, and was collected by the said Edwards as such collector of internal revenue from the American Can Company.

3. The Commissioner of Internal Revenue ruled and determined that the basis upon which the plaintiff and its said affiliated companies kept their accounts and made their Federal income and excess-profits tax returns for 1917 did not clearly reflect their incomes; that their incomes for 1917 should not be determined upon such basis; and that their income and excess-profits taxes for 1917 should not be computed upon their incomes as returned.

4. The gross amount of the income of the plaintiff received within the year 1917 from all sources was $241,246.48. The amount of the ordinary and necessary expenses paid by the plaintiff within
248 the year 1917 in the maintenance and operation of its business and properties was $211,806.34. The amount of the losses actually sustained and charged off by the plaintiff within the year 1917 and not compensated by insurance or otherwise was $16,352.21. The amount of the taxes paid by the plaintiff within the year 1917 imposed by the authority of the United States (except income and excess-profits taxes) or of its Territories or possessions, or any foreign country, or by the authority of any State, county, school district, or

municipality, or other taxing subdivision of any State, not including those assessed against local benefits, was $6,531.45. The amount of the net income of the plaintiff for the year 1917, determined upon the basis of actual receipts and disbursements by deducting from the gross amount of its income received within the year from all sources all such expenses and taxes paid within the year and all such losses actually sustained and charged off within the year, was $6,556.48. The amounts above mentioned for expenses, losses, and taxes include only expenses, losses, and taxes which are described in section 12 (a) of Title I of the act of Congress entitled, "An act to increase the revenue and for other purposes," approved September 8, 1916, as amended by the act of Congress, entitled, "An act to provide revenue to defray war expenses and for other purposes," approved October 3, 1917, subject to the limitations and provisos therein mentioned. The amount of the net income of the plaintiff for the year 1917, ascertained upon the basis and in the manner provided in said section 12 (a) as so amended, was $6,556.48.

5. The total amount of the Federal income taxes for 1917 payable by the plaintiff upon $6,556.48 of net income was $393.39. The American Can Company has paid to the defendant all Federal excess-profits taxes for 1917 which have been assessed against or payable by the plaintiff or any of its said affiliated companies.

949 6. No part of the amount which the plaintiff has paid, or which William H. Edwards as collector of internal revenue of the United States has collected from the plaintiff as and for income taxes for 1917, has been refunded or repaid to the plaintiff or credited against any income, war-profit, or excess-profits tax or instalment thereof due from or payable by the plaintiff.

Conclusions of law

From the foregoing the court concludes:

1. On or about June 14, 1918, the plaintiff paid, and William H. Edwards as collector of internal revenue of the United States, collected from the plaintiff as and for Federal income taxes for the year 1917, $5,893.80 in excess of the amount which was legally payable and collectible. Said amount was assessed and collected erroneously, illegally, wrongfully, and without authority.

2. The plaintiff is entitled to judgment against the defendant for $5,893.80 with interest at the rate of 6% per annum from June 14, 1918.

Let judgment be entered accordingly.

Dated August 16, 1927.

J. L. BODINE, *District Judge.* [L. S.]

Mr. HENDLER. Exception to each of foregoing findings of fact and conclusions of law.

Exceptions allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

250 In United States District Court

DETROIT CAN COMPANY, PLAINTIFF

AGAINST

THE UNITED STATES, DEFENDANT

Judgment

Filed August 16, 1927

The above-entitled cause having duly come on to be heard before the above-entitled court, Honorable Joseph L. Bodine, judge thereof, presiding, and all parties having been present and represented by counsel and the cause having been heard and thereafter the court having caused a written opinion to be filed in the cause setting forth the specific findings by the court of the facts therein and the conclusions of the court upon all questions of law involved in the case, and having rendered judgment thereon,

Now, therefore, by virtue of the law and by reason of the premises aforesaid,

It is considered and adjudged that the plaintiff herein do have and recover of and from the defendant the sum of $9,135.39, being the sum of $5,893.80 with interest at the rate of six per centum (6%) per annum from June 14, 1918.

Dated August 16, 1927.

J. L. BODINE, *Judge.* [L. S.]

MR. HENDLER. Exception.

Exception allowed and sealed accordingly.

J. L. BODINE, *Judge.* [L. S.]

251 In United States District Court

DETROIT CAN COMPANY, PLAINTIFF

VS.

THE UNITED STATES, DEFENDANT

Order extending term

Filed September 17, 1927

This matter being opened to the court by Walter G. Winne, United States attorney for the District of New Jersey (by James S. Turp, Assistant United States Attorney):

It is on this 12th day of September, A. D. 1927, ordered that the April term of this court be and the same hereby is extended for a period of thirty days for the purpose of settling and signing bill of exceptions herein.

J. L. BODINE, *Judge.* [L. S.]

Entered Sept. 17th, 1927.

252 In United States District Court

DETROIT CAN COMPANY, PLAINTIFF

vs.

THE UNITED STATES, DEFENDANT

Order extending term

Filed October 11, 1927

This matter being opened to the court by Walter G. Winne, United States attorney for the District of New Jersey (by James S. Turp, Assistant United States Attorney), and good cause being shown therefore:

It is on this 11th day of October, A. D. 1927, ordered that the April term of this court be and the same hereby is extended for an additional period of thirty days from October 12, 1927, for the purpose of settling and signing bill of exceptions herein.

J. L. BODINE, *Judge.* [L. S.]

253 In United States District Court

THE UNITED STATES, PLAINTIFF IN ERROR, (DEFENDANT BELOW)

vs.

DETROIT CAN COMPANY, DEFENDANT IN ERROR (PLAINTIFF BELOW)

Petition for writ of error

Filed Nov. 9, 1927

To the honorable judges of the United States District Court for the District of New Jersey.

And now comes the United States, defendant in the above entitled cause, by Walter G. Winne, United States attorney for the District of New Jersey, and says that on the 16th day of August, 1927, the court entered judgment herein against defendant, for the sum of nine thousand one hundred thirty-five dollars and thirty-nine cents ($9,135.39), in which final judgment and the proceedings had prior thereto in this cause, certain errors were committed to the prejudice of this defendant, all of which will more fully appear in the assignments of error filed with this petition.

254 Wherefore, this defendant prays that a writ of error may issue in this behalf to the United States Circuit Court of Appeals for the Third Circuit for the correction of the error so complained of, and that a transcript of the record of the proceedings

and papers in this cause, duly authenticated, may be sent to the said court.

WALTER G. WINNE,
United States Attorney,
By JAS. S. TURP,
Assistant U. S. Attorney,
Attorneys for Defendant (Plaintiff in Error).

In United States District Court

THE UNITED STATES, PLAINTIFF IN ERROR, (DEFENDANT BELOW)

vs.

DETROIT CAN COMPANY, DEFENDANT IN ERROR (PLAINTIFF BELOW)

Assignment of errors

Filed Nov. 9, 1927

And the said United States, defendant and plaintiff in error, by Walter G. Winne, United States attorney for the District of
255 New Jersey, comes and says that in the record of the proceedings and in the findings of the court in said cause by the said District Court of the United States for the District of New Jersey, there is manifest error in this, to wit:

1. That the court erred in admitting statement computed by the plaintiff and marked "Exhibit P–7."

2. That the court erred in admitting statement computed by plaintiff and marked "Exhibit P–8."

3. That the court erred in admitting statements computed by plaintiff and marked "Exhibits P–9 and P–9a."

4. That the court erred in admitting statement computed by the plaintiff and marked "P–11."

5. That the court erred in excluding answer to question of the witness Mr. Green as to whether it would be possible to show the income of American Can Company by wholly disregarding the opening inventory and deducting the inventory of the goods on hand and in process at the close of 1917 assuming that all of the earnings of the American Can Company had been invested in raw material during the year 1917.

6. That the court erred in excluding answer to question of the witness Mr. Green as to whether the company having kept the books of account on the accrual basis and having made returns for the years 1916, 1917, and 1918 on the accrual basis, the so-called cash receipts and disbursements basis, without taking into account the opening and closing inventories for the year 1917, would correctly reflect the income of the American Can Company during the year 1917.

7. That the court erred in excluding statements computed by the defendant and marked for identification "Exhibits D–2 and D–3."

8. That the court erred in denying the motion of defendant for judgment.

256 9. That the court erred in each and every of his findings of fact and conclusions of law.

10. That the court erred in denying the requests for findings of fact and conclusions of law presented by defendant.

11. That the court erred in fiinding judgment for the plaintiff.

Dated at Trenton, New Jersey, this 9th day of November, 1927.

WALTER G. WINNE,
United States Attorney.

In United States District Court

THE UNITED STATES, PLAINTIFF IN ERROR (DEFENDANT BELOW)

vs.

DETROIT CAN COMPANY, DEFENDANT IN ERROR (PLAINTIFF BELOW)

Order allowing writ of error

Filed Nov. 9, 1927

This 9th day of November, 1927, came the defendant, the United States of America, by Walter G. Winne, United States Attor-
257 ney, and filed herein and presented to the court his petition praying for the allowance of a writ of error intended to be urged by him, praying also that the transcript of record and proceedings and papers, upon which the judgment herein was rendered, duly authenticated, may be sent to the United States Circuit Court of Appeals for the Third Circuit, and that such other and further proceedings may be had as may be proper in the premises.

On consideration whereof the court has allowed the writ of error.

J. L. BODINE, *Judge.* [L. S.]

In United States Circuit Court of Appeals, for the Third Circuit

Writ of error

Filed Nov. 9, 1927

THE UNITED STATES OF AMERICA,
Third Judicial Circuit, ss:

The President of the United States to the Honorable Judges of the District Court of the United States for the District of New Jersey, Greeting:

Because in the record and proceedings, as also in the rendi-
258 tion of the judgment, of a plea which in the said District Court, before you, or some of you, between Detroit Can Company, plaintiff, and the United States, defendant, a manifest error hath happened, to the great damage of the said United States, de-

fendant, as by his complaint appears, we being willing that error, if any hath been, should be duly corrected and full and speedy justice done to the parties aforesaid in this behalf, do command you, if judgment be therein given, that then under your seal, distinctly and openly you send the record and proceedings aforesaid, with all things concerning the same, to the United States Circuit Court of Appeals for the Third Circuit, together with this writ, in said circuit on the 8th day of December next, so that you have the same at Philadelphia, in said circuit on the 8th day of December next, in the said Circuit Court of Appeals, to be then and there held, that the record and proceedings aforesaid being inspected, the said Circuit Court of Appeals may cause further to be done therein to correct that error, what of right and according to laws and customs of the United States, should be done.

Witness, the Honorable William Howard Taft, Chief Justice of the United States, this 9th day of November, A. D. 1927.

[SEAL.] GEORGE T. CRANMER,

Attest:

_____ _____,

Clerk of the United States District Court, District of New Jersey.

By CHARLES S. CHEVRIER,

Deputy.

259 [Citation in usual form showing service on John J. Treacy, filed Nov. 15, 1927, omitted in printing.]

260 In United States District Court

DETROIT CAN COMPANY, PLAINTIFF vs. THE UNITED STATES, DEFENDANT	In Equity

Stipulation as to Record

It is hereby stipulated and agreed, that the foregoing is a true transcript of the record of the said District Court in the above-entitled matter as agreed on by the parties for the purposes of this appeal.

Dated Oct. 18th, 1928.

JOHN J. TREACY,
Attorney for Plaintiff.
JAMES W. MCCARTHY,
United States Attorney,
Attorney for Defendant.

261 [Clerk's certificate to foregoing transcript omitted in printing.]

262 [Minute entry of argument and submission, Dec. 12, 1928, omitted in printing.]

263 In the United States Circuit Court of Appeals for the Third Circuit

Nos. 3750, 3751, 3752. October Term, 1928

AMERICAN CAN COMPANY

v.

UNITED STATES

DETROIT CAN COMPANY

v.

UNITED STATES

MISSOURI CAN COMPANY

v.

UNITED STATES

On appeal from the District Court of the United States for the District of New Jersey

Before BUFFINGTON, WOOLLEY, and DAVIS, circuit judges

Opinion Filed March 5, 1929

DAVIS, circuit judge:

This is an appeal from judgments of the district court ordering refund of income taxes alleged to have been illegally assessed and collected by the Commissioner of Internal Revenue.

The American Can Company owns all, or substantially all,
264 of the stock of the Missouri Can Company, the Detroit Can Company and ten other companies. These were referred to in the trial as the plaintiff and its domestic affiliated corporations. They kept their accounts for the year 1917 upon the accrual basis, accruing their receipts and disbursements. In that year, they valued their stock of tin plate carried in their inventories at a constant figure regardless of changes in the cost or market value. Their stock other than tin plate, they valued at cost or market value, whichever was lower. In 1916, the price of tin plate was $3.60 per box, but in 1917, it advanced to $7.00 per box and so in that year the plaintiffs adopted the system or basis of a constant, invariable figure in their inventory of tin plate supply, called the "inventory constant." The defendant says: that this had the effect of increasing the cost of goods sold in 1917 to the extend of $3.40 per box;

that the tin plate on hand at the close of 1916, which cost plaintiffs $3.60 per box, was used by them in filling their contracts during 1917 and was charged into cost at $7.00 per box and consequently in addition to their normal profit on manufacture and sale they made a substantial inventory profit which was not reported in their income.

The commissioner had two audits made of their returns and concluded that this accrual basis employed by the plaintiffs did not reflect their true net income and so in his redetermination, he calculated the cost of tin plate at $3.60 per box for the entire year of 1917. This increased the consolidated net income from $17,994,400.46, shown in the first return, to $24,949,668.51.

The plaintiffs contend that this method or basis employed by the commissioner was arbitrary and not authorized by statute; that since the accrual basis used by them in keeping their accounts admittedly did not reflect their true net income, the only other basis
265 on which their returns could be made and taxes assessed by the commissioner was that of "actual receipts and disbursements," and this basis the commissioner did not use; that as a result there was assessed against, and collected from, the American Can Company $2,705,501.71, the Missouri Can Company, $7,763.65 and the Detroit Can Company, $5,893.80, in excess of the taxes which were legally payable and collectible as income and excess profits taxes for 1917, when ascertained and assessed upon the basis of actual receipts and disbursements.

The learned trial judge, sitting by agreement without a jury, found as admitted, that the basis on which the plaintiffs kept their inventory and made their return did not reflect their true net income and that the commissioner changed this basis to some other basis than that of receipts and disbursements, without statutory authority. He accordingly entered judgment for the plaintiffs for the amounts demanded with interest.

The stock other than tin plate was valued at its cost or market price, whichever was lower, and the reason why the basis used by the plaintiffs in making their return did not reflect their true net income was because of this "inventory constant," $7.00 per box, used in making the inventory of the stock of tin plate, regardless of cost or market value. When this was changed and $3.60 was used instead, the basis of making their inventory was changed so that the cost of finished products was decreased and the net income increased. The change by the commissioner was not the mere or incidental change or correction of a figure in a system, but the change of a system, from one basis to a different basis.

Since the basis used by the plaintiffs did not reflect their true income, to what basis could the commissioner legally change?

266 Section 13 (d) of Title I of the revenue act of 1917 provides that:

"(d) A corporation, joint-stock company or association, or insurance company, keeping accounts upon any basis other than that

of actual receipts and disbursements, unless such other basis does not clearly reflect its income, may, subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned."

Accordingly if a corporation has kept its accounts upon a basis other than that of "actual receipts and disbursements," it may, subject to regulations of the commissioner with the approval of the Secretary of the Treasury, make its return upon that basis and the tax on its income shall be computed as so returned, if it clearly reflects its income; but if it does not clearly reflect its income, then the tax must be computed on the cash, or receipts and disbursements, basis as prescribed in section 12, which provides that:

"Sec. 12. (a) In the case of a corporation, joint-stock company or association, or insurance company, organized in the United States, such net income shall be ascertained by deducting from the gross amount of its income received within the year from all sources—

"First. All the ordinary and necessary expenses paid within the year in the maintenance and operation of its business and properties * * *.

"Second. All losses actually sustained and charged off within the year * * *.

"Third. The amount of interest paid within the year * * *.

"Fourth. Taxes paid within the year * * *."

267 This is the receipts and disbursements, or cash, basis and the tax must be asssessed on this basis. Gould v. Gould, 245 U. S. 151; United States v. Anderson et al., 269 U. S. 422, 441; Iselin v. United States, 270 U. S. 245; United States v. Field, 255 U. S. 257; Smietanka v. First Trust & Savings Bank, 257 U. S. 602; Shwab v. Doyle, 258 U. S. 529.

In the Act of 1918 Congress expressly conferred upon the commissioner power to redetermine the income on such basis as he might prescribe, but he had no such power under prior acts and if the accrual or other basis used by the taxpayer in making his return did not reflect the true net income, he must use the cash basis.

As the basis which the commissioner used in redetermining the tax was not authorized in the act of 1917, it was contrary to law as found by the district court. The tax which the district court ordered refunded was the excess which the plaintiffs paid, computed on the receipts and disbursements basis, and was right in law and fact.

The judgments are affirmed.

A true copy:

Teste:

_____ _____,

Clerk of the United States Circuit Court of Appeals for the Third Circuit.

268 In United States Circuit Court of Appeals, Third Circuit

No. 3750 (List No. 136). October term, 1928

UNITED STATES, PLAINTIFF IN ERROR

vs.

AMERICAN CAN COMPANY, DEFENDANT IN ERROR

Judgment

Filed Mar. 5, 1929

In error to the District Court of the United States for the District of New Jersey

This cause came on to be heard on the transcript of record from the District Court of the United States for the District of New Jersey, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the judgment of the said District Court in this cause be, and the same is hereby affirmed.

Philadelphia, March 5, 1929.

J. WARREN DAVIS, *Circuit Judge.*

[File indorsement omitted.]

269 In United States Circuit Court of Appeals, Third Circuit

No. 3751 (List No. 137). October term, 1928

UNITED STATES, PLAINTIFF IN ERROR

vs.

DETROIT CAN COMPANY, DEFENDANT IN ERROR

Judgment

Filed Mar. 5, 1929

In error to the District Court of the United States for the District of New Jersey

This cause came on to be heard on the transcript of record from the District Court of the United States for the District of New Jersey, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the judgment of the said District Court in this cause be, and the same is hereby affirmed.

Philadelphia, March 5, 1929.

J. WARREN DAVIS, *Circuit Judge.*

[File indorsement omitted.]

270 In United States Circuit Court of Appeals, Third Circuit

No. 3752 (List No. 138.) October term, 1928

UNITED STATES, PLAINTIFF IN ERROR

vs.

MISSOURI CAN COMPANY, DEFENDANT IN ERROR

Judgment

Filed Mar. 5, 1929

In error to the District Court of the United States for the District of New Jersey

This cause came on to be head on the transcript of record from the District Court of the United States for the District of New Jersey, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the judgment of the said District Court in this cause be, and the same is hereby affirmed.

Philadelphia, March 5, 1929.

J. WARREN DAVIS, *Circuit Judge.*

[File indorsement omitted.]

271 [Clerk's certificate to foregoing transcript omitted in printing.]

272 In Supreme Court of the United States

No. 128. October term, 1929

THE UNITED STATES, PETITIONER

vs.

AMERICAN CAN COMPANY

Order allowing certiorari

Filed October 14, 1929

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

273 In Supreme Court of the United States

No. 129 October term, 1929

THE UNITED STATES, PETITIONER

vs.

MISSOURI CAN COMPANY

Order allowing certiorari

Filed October 14, 1929

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

274 In Supreme Court of the United States

No. 130. October term, 1929

THE UNITED STATES, PETITIONER

vs.

DETROIT CAN COMPANY

Order allowing certiorari

Filed October 14, 1929

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Indorsement on cover:] File Nos. 34,259, 34,260, 34,261. U. S. Circuit Court of Appeals, Third Circuit. Term No. 128, the United States, petitioner, vs. American Can Company; term No. 129, the United States, petitioner, vs. Missouri Can Company; term No. 130, the United States, petitioner vs. Detroit Can Company. Petition for writs of certiorari and exhibit thereto. Filed June 4th, 1929. File Nos. 34,259, 34,260, 34,261.

U. S. GOVERNMENT PRINTING OFFICE: 1929

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CHARLES ELMORE CROPLEY
CLERK

Nos. —, —,

In the Supreme Court of the United States

OCTOBER TERM, 1928

THE UNITED STATES, PETITIONER

v. 128

AMERICAN CAN COMPANY

THE UNITED STATES, PETITIONER

v. 129

MISSOURI CAN COMPANY

THE UNITED STATES, PETITIONER

v. 130

DETROIT CAN COMPANY

PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF

U. S. GOVERNMENT PRINTING OFFICE: 1929

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In the Supreme Court of the United States

OCTOBER TERM, 1928

No. ——

THE UNITED STATES, PETITIONER

v.

AMERICAN CAN COMPANY

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MISSOURI CAN COMPANY

No. ——

THE UNITED STATES, PETITIONER

v.

DETROIT CAN COMPANY

PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF

PETITION

The Solicitor General, on behalf of the United States, prays that writs of certiorari issue to re-

view the judgments of the Circuit Court of Appeals for the Third Circuit entered in the above-entitled cases on March 5, 1929, affirming the judgments of the District Court of the United States for the District of New Jersey.

STATEMENT

The American Can Company and its subsidiaries, Missouri Can Company and Detroit Can Company, respondents herein, are engaged in the business of manufacturing and selling cans and other containers. They kept their accounts, made their returns, and paid their income and excess-profits taxes for the year 1917 totaling $3,266,499.86 upon the accrual basis. (R. 3–4, 174–175, 194–195, 211–212, 228–229, 246–247.) Additional assessments were thereafter made against the parent company totaling $1,953,480.79 (R. 5), and were paid to the then collector William H. Edwards, who had collected the original assessments. Thereafter a final audit resulted in further additional assessments which have given rise to this litigation based upon the following facts:

Respondents, in the conduct of their business, were required to keep on hand large stocks of tin plate, which was the most important material used by them. (R. 194, 229.) The market price of tin plate rose sharply in the early part of 1917 from $3.60 per base box to $7. Respondents took advantage of this sharp increase in value of stocks on hand by writing up as of January 1, 1917, to

$7 per base box, their opening inventories of tin plate, which had cost them but $3.60 per box, and transferring so much of the inventory write-up as was claimed to represent respondents' normal stocks of tin plate to the so-called "inventory constant" accounts set up for the first time in that year.

[The above facts showing the manner in which respondents' books of account reflected this write up of tin plate in inventory and transfer to their "inventory constant" accounts, and the reasons therefor, are not included in the findings made by the District Court, but are supported by uncontradicted evidence in the record (R. 50, 81, 83) which has been adopted by the Circuit Court of Appeals in its opinion (R. 261–262) as proven facts.]

This had the effect of increasing the cost of goods sold as returned by the respondents and resulted in an understatement of net income to the extent of the amounts credited to their respective "inventory constant" accounts. The net income of the American Can Company was thus understated by $4,722,500 (R. 13), the net income of the Missouri Can Company by $168,500 (R. 14), and the net income of the Detroit Can Company by $70,000 (R. 14).

The Commissioner of Internal Revenue eliminated this artificial inflation of the cost of goods sold (R. 13–14), increased respondents' net income by the amounts in the "inventory constant" accounts, and made further additional assessments as follows: American Can Company $3,383,481.46 (R.

6); Missouri Can Company $10,110 (R. 195); Detroit Can Company $4,200 (R. 230). Respondents filed claims to abate such further additional assessments and filed claims for refund of so much of the taxes theretofore paid as exceeded what they contended was their true tax lability computed on the cash receipts and disbursements basis. The grounds set forth in the claims, which are also the grounds upon which these suits are based, were that the Commissioner, in correcting the valuation of inventories used in the computation of the cost of goods sold, rejected the basis upon which their accounts were kept and their returns filed, and that as the result of the action of the Commissioner, they became entitled under the provisions of Section 13 (d) of the Revenue Act of 1916, to have their income computed on the cash receipts and disbursements basis, and that on such basis, respondents' tax liability was not only less than that computed by the Commissioner but was less by $2,719,159.16 (R. 162–163) than the taxes paid by them on their returns as filed.

The District Court for the District of New Jersey upheld these contentions (R. 160–165) and allowed respondents a recovery of the amount of taxes paid to William H. Edwards, Collector, in excess of the amounts found by the court to be their tax liability computed on the cash receipts and disbursements basis. (Exhibit P–7 (R. 128), Exhibit

P–8 (R. 149, 150), Exhibit P–10 (R. 153); R. 181, 214, 249.)

Respondents' income on the cash basis adopted by the court was computed without the use of inventories and does not correctly reflect the gross amount of income and the cost and expenses properly attributable to the production of that income. It amounts to no more than the statement showing the excess of income receipts over income expenditures, each class having no necessary relation to the other. The District Court has not made findings that the computation of income on the cash basis adopted by it was arrived at without the use of inventories, but this fact was established by the testimony of one of respondents' witnesses (R. 84), and requests for such a finding were made by the Government in each case and were denied (R. 170, 207, 242).

The cases were tried together in the District Court. Upon the conclusion of the trials in the District Court the Government made timely motions for judgments in its favor, which were denied and exceptions duly taken and allowed. (R. 99.) Requested findings of fact were made and filed by the Government in each case, and exceptions duly taken and allowed to the court's refusal to make the findings requested. (R. 166–172, 203–209, 238–244.) Timely exceptions were also taken and allowed to the findings of fact and conclusions of law as made and filed by the District Court in each case. (R. 174–181, 211–214, 246–249.)

The Circuit Court of Appeals for the Third Circuit affirmed the judgments of the District Court in an opinion reported in 31 F. (2d) 730, and the United States by this petition seeks a review of that action by this Court.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

I. In holding that the action of the Commissioner in these cases amounted to a rejection of the accrual basis upon which basis the respondents kept their accounts and upon which their returns were made so as to entitle respondents to have their income for the year 1917 computed on the basis of cash receipts and disbursements.

II. In holding that the respondents' income computed upon a cash receipts and disbursements basis could be correctly determined without showing by the use of inventories the cost of goods sold.

III. In holding that respondents were entitled, as a matter of right, to have their taxes computed on the basis of cash receipts and disbursements in the absence of a finding that the accrual basis, which the Commissioner is said to have rejected, did not in fact reflect their true income.

REASONS FOR GRANTING THE WRITS

The cases are of vital importance to the Government and to the public, not only because of the large amounts involved, but also because they present an important question of Federal law of general application as to the extent to which the Com-

missioner of Internal Revenue may go in the correction of returns without departing from the statutory precept regarding the accounting basis upon which returns must be made.

If the decision of the Circuit Court of Appeals, that the *mere* correction by the Commissioner of respondents' inventory valuation of tin plate amounted to a rejection of the basis upon which respondents' books of account were kept and their returns filed is allowed to become settled law, much confusion will arise in the future as to how far the Commissioner may go in correcting returns filed in accordance with a particular system of accounting so as to prevent a taxpayer from becoming entitled to have his income computed under the cash receipts and disbursements basis.

The decision of the Circuit Court of Appeals is in conflict with the decision of the Circuit Court of Appeals for the Sixth Circuit in the case of *Aluminum Castings Co.* v. *Routzahn,* 31 F. (2d) 669, wherein the Commissioner's right to make adjustments in a return on the accrual basis filed under Section 13 (d) of the Revenue Act of 1916, here involved, was upheld.

The decision of the Circuit Court of Appeals is also in conflict with the decision of this Court in *Doyle* v. *Mitchell Brothers Co.,* 247 U. S. 179, in that respondents' income on the so-called cash receipts and disbursements basis, which the Circuit Court of Appeals adopted as correct, was arrived at without regard to inventories. The Circuit Court

of Appeals in thus determining net income as the excess of income receipts over income expenditures, without taking into consideration the cost of goods sold which produced the income has not followed the rule laid down by this Court in the cases of *United States* v. *Anderson,* 269 U. S. 422, and *American National Co.* v. *United States,* 274 U. S. 99. In those cases this Court has recognized that the basis of cash receipts and disbursements will not properly reflect the true income of manufacturing and mercantile concerns.

The decision of the Circuit Court of Appeals is contrary to the decisions of the District Court for the Southern District of New York in four cases (now pending in the Circuit Court of Appeals for the Second Circuit) brought by the respondent, American Can Company, and its subsidiaries, against Bowers, Collector, to recover further additional assessments paid by the same taxpayer for the same taxable year and raising precisely the same questions.

Wherefore, it is respectfully submitted that this petition for writs of certiorari to review the judgments of the Circuit Court of Appeals for the Third Circuit should be granted.

CHARLES E. HUGHES, JR.,
Solicitor General.

JUNE, 1929.

BRIEF IN SUPPORT OF THE PETITION

OPINIONS BELOW

The opinion of the District Court for the District of New Jersey (R. 160–165) is reported in 20 F. (2d) 970. The opinion of the United States Circuit Court of Appeals (R. 261–263) is reported in 31 F. (2d) 730.

JURISDICTION

The judgments of the United States Circuit Court of Appeals were entered on March 5, 1929. (R. 263–264.) The jurisdiction of this Court rests on the provisions of Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the correction by the Commissioner of Internal Revenue of the valuation of the inventories of tin plate in respondents' returns made on the accrual basis constituted such a rejection of the basis on which respondents' accounts were kept as to render it necessary under Section 13 (d) of the Revenue Act of 1916 to compute the income on the basis of cash receipts and disbursements.

2. Assuming because of the action of the Commissioner respondents are entitled to have their income computed on the basis of cash receipts and disbursements, can respondents' income be cor-

rectly computed on such basis without the use of inventories?

3. Assuming that the Commissioner in changing the valuation of respondents' inventories has rejected respondents' accrual basis of accounting, does such a rejection made by the Commissioner herein in determining that an additional assessment was due for the year 1917 entitle respondents to a recovery of taxes paid on their returns filed on the accrual basis in the absence of a finding that such accrual basis did not reflect their true income?

STATUTES AND REGULATIONS INVOLVED

The pertinent portion of the Revenue Act of 1916, c. 463, 39 Stat. 756, 771, reads:

> SEC. 13. (a) The tax shall be computed upon the net income, as thus ascertained, * * *;
>
> (d) A corporation, joint-stock company or association, or insurance company, keeping accounts upon any basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect its income, may, subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned; * * *.

The pertinent portion of the Revenue Act of 1917, c. 63, 40 Stat. 300, 305, reads:

SEC. 206. That for the purposes of this title the net income of a corporation shall be ascertained and returned * * * (c) for the taxable year upon the same basis and in the same manner as provided in Title I of the Act entitled "An Act to increase the revenue, and for other purposes," approved September eighth, nineteen hundred and sixteen, as amended by this Act * * *.

Treasury Decision No. 2609 promulgated December 19, 1917:

(1) For the purposes of income and excess-profits tax returns, inventories of merchandise, etc., and of securities will be subject to the following rules:

A. Inventories of supplies, raw materials, work in process of production, and unsold merchandise must be taken either (a) at cost or (b) at cost or market, whichever is lower, provided that the method adopted must be adhered to in subsequent years, unless another be authorized by the Commissioner of Internal Revenue.

B. A dealer in securities who, in his books of account, regularly inventories unsold securities on hand either (a) at cost or (b) at cost or market price, whichever is lower, may, for purposes of income and excess-profits taxes, make his return upon the basis upon which his accounts are kept; provided that a description of the method employed shall be included in or attached to the return, that all the securities must be inven-

toried by the same method, and that such method must be adhered to in subsequent years, unless another be authorized by the Commissioner of Internal Revenue.

C. Gain or loss resulting from the sale or disposition of assets inventoried as above must be computed as the difference between the inventory value and the price or value at which sold or disposed of.

(2) In all other cases inventories must be taken at cost or at value as of March 1, 1913, as the case may be.

STATEMENT

A statement of the facts and the errors relied on will be found in the petition.

ARGUMENT

The amount of tax for 1917 in dispute between the American Can Company and its subsidiaries and the United States is approximately $8,000,000. The entire dispute arises out of the Commissioner's treatment of the inventory account. A part of the disputed taxes in a sum approximating $4,000,000 was paid to a collector in the District of New York who was no longer in office at the time these suits were brought, and a part was paid to the incumbent collector in the said district. These cases were instituted in New Jersey to recover a part of the taxes paid to the late collector on the original returns and on the additional assessment made by the Commissioner September 21, 1920. (R. 5.)

Similar suits brought against Collector Frank K. Bowers in the Southern District of New York to recover the further additional assessments (R. 6, 195), which were paid to him under protest upon the denial of the claims in abatement (R. 7, 195–196), and which thus involve the same tax liability of the same taxpayers, for the same year, and raise precisely the same questions, have resulted in judgments in favor of the Collector. The New York District Court held that the Commissioner in his final audit did not reject the accrual basis but correctly determined respondents' true income on the basis upon which their accounts were kept. The very anomalous situation is thus presented of the action of the Commissioner, with respect to the same tax liability, of the same taxpayers, for the same tax year, being valid in one jurisdiction and invalid in another. The opinion of the District Court is not officially reported as yet and is printed as an appendix to this brief. The New York judgments are now pending on appeal before the Circiut Court of Appeals for the Second Circuit and have been set for argument on October 7, 1929.

The cases here involve the power of the Commissioner to make corrections in returns filed under Section 13 (d) of the Revenue Act of 1916. It is the contention of the petitioner that the corrections made by the Commissioner in these cases in no wise affected the basis upon which the income was returned, and that his action did not give respond-

ents the right to have their income computed on the cash receipts and disbursements basis as was held by the courts below.

The respondents made their returns for income and excess profits tax purposes on what is called the accrual basis, treating accounts receivable as equivalent of receipts and accounts payable as equivalent of disbursements, and they valued their inventory on the basis of cost or market value, whichever was lower, except for their normal stocks of tin plate, which they valued at a constant figure irrespective of change in market value. This was accomplished by an arbitrary write-up in January, 1917, of opening inventory of tin plate costing $3.60 per box to current market value of $7 per box and by transferring so much of the write-up as covered normal stock of tin plate to an "inventory constant" account opened for the first time in that year.

This arbitrary valuation of the inventory of tin plate by respondents resulted in an understatement of respondents' net income, which was arrived at in violation of the provisions of Treasury Decision No. 2609, promulgated on December 19, 1917, which governed returns filed for the year 1917, and required that all goods in inventory be carried at cost or market, whichever was lower.

The Commissioner, in his audit of respondents' returns, adjusted the inventory accounts to conform to the requirements of this valid regulation (*United States* v. *Kemp,* 12 F. (2d) 7; certiorari

denied, 273 U. S. 703), and correctly determined respondents' gross income and expenses incident to the production of that income. *United States* v. *Anderson,* 269 U. S. 422; *American National Co.* v. *United States,* 274 U. S. 99.

The decision of the Circuit Court of Appeals rests on the view that respondents' method of valuing its tin plate in its inventories gives rise to a statutory basis of keeping accounts distinct in itself and different from a strict accrual basis. This is made clear from its decision, wherein that court said (R. 262):

> The stock other than tin plate was valued at its cost or market price, whichever was lower, and the reason why the basis used by the plaintiffs in making their return did not reflect their true net income was because of this "inventory constant," $7.00 per box, used in making the inventory of the stock of tin plate regardless of cost or market value. When this was changed and $3.60 was used instead, the basis of making their inventory was changed so that the cost of finished products was decreased and the net income increased. The change by the commissioner was not the mere or incidental change or correction of a figure in a system, but the change of a system from one basis to a different basis.

Based upon this view the Circuit Court of Appeals has held that the Commissioner's action in correcting respondent's valuation of tin plate in

inventory amounted to a rejection of the basis upon which their accounts were kept and their returns filed, and that the basis actually used by the Commissioner in redetermining the tax of respondents for the year 1917 was not authorized by the Act of 1917 (1916 Act as amended) and was contrary to law. In conclusion that court held that if the basis on which returns were made did not reflect true income, which it assumes to be the case because of the Commissioner's action in correcting it, the Commissioner must use the cash basis.

Under this construction of Section 13 (d) the Commissioner in most cases will be compelled to accept returns as filed without change or correction and compute taxes on the income *as returned,* otherwise taxpayers will become entitled to have their income computed on the cash receipts and disbursements basis, which basis, as was recognized by this Court in the cases of *United States* v. *Anderson, supra,* and *American National Co.* v. *United States, supra,* will not properly reflect the true income of manufacturing and mercantile concerns. It is therefore submitted that the Circuit Court of Appeals has misconstrued the true meaning of the provisions of this section.

The term "basis" as used in Section 13 (d) has regard to the principle on which accounts are kept, that is, as to when income is deemed to have been received and disbursements deemed to be made. It has nothing whatever to do with the number or vari-

ety of accounts used by a corporation in its bookkeeping methods nor with the opening of new accounts. It refers to the theory and practice upon which accounts are kept—that is, whether income and expenditures are treated as having been received and disbursed only when cash is actually received and disbursed or whether receipts are treated as received when they accrue and disbursements treated as made when they are incurred. That Congress had these two fundamental bases of accounting primarily in mind when it enacted subdivision (d) of Section 13 is evident from the report of the Ways & Means Committee of the House (House Report No. 922, Sixty-fourth Cong., 1st sess.) wherein it is said (p. 4):

> * * * As two systems of bookkeeping are in use in the United States, one *based* on the cash or receipt basis and the other on the accrual basis, it was deemed advisable to provide in the proposed measure that an individual or corporation may make return of income on either the cash or accrued basis, if the *basis* selected clearly reflects the income. (Italics supplied.)

It is obvious that if one corporation values its inventory on the basis of cost or market, whichever is lower, while another company in the same business in making up its inventory uses a different valuation, it would be absurd to hold because of such difference in the method of valuing the goods that those corporations employed different bases of

accounting. It would likewise be unsound to hold that if the Commissioner were to change the values ascribed by the second company to its inventory to comport with cost he thereby changed the basis on which the taxpayer kept its books and made its return.

In this case respondents treated the "inventory constant" accounts as a present expense chargeable against current income; the Commissioner (following *United States* v. *Anderson, supra,* and *American National Co.* v. *United States, supra*), treated it as a reserve set up out of current income to meet anticipated future losees not sustained in the current year. Whichever treatment is proper, it is obvious that the basis upon which the accounts were kept and returns made was not changed. All that the Commissioner did was to disallow as a deduction an item of alleged expense shown by respondents' books which was not in fact incurred in the taxable year. This obviously was not a change of respondents' basis, but merely a correction of the returns to conform to that basis. This is clear from the fact that the Commissioner's action did not result in any inconsistent treatment of any of the items in respondents' returns, all of the items being treated throughout on the accrual basis. The question here does not involve a change of the taxpayer's books or accounts but merely an interpretation of them for the purposes of determining how much income they show to have been earned during the year 1917.

A similar question was involved in the case of the *Aluminum Castings Co.* v. *Routzahn,* 31 F. (2d) 669, wherein the Circuit Court of Appeals for the Sixth Circuit, in a well-reasoned opinion, held adversely to the decision of the Circuit Court of Appeals herein. In that case the court rejected taxpayer's contention that it kept its books of account and filed its return on the cash receipts and disbursements basis and was entitled to have its income computed on the basis on which it kept its accounts and, holding that taxpayer's returns for the years 1916 and 1917 were made on the accrual basis, approved the action of the Commissioner in disallowing for the year 1917 a deduction for munitions taxes paid in 1917 but which had accrued in 1916. Since taxpayer in that case had adopted the method of treating accounts payable as expenditures as of the time of entry upon its books rather than when the same accrued, this bookkeeping departure from the strict accrual basis created a system just as distinctive as that created by the method in which respondents valued their tin plate in their inventories.

But if the income is to be determined on the basis of cash receipts and disbursements, it is not properly disclosed by respondents' calculation. In that calculation the deduction taken for expenses includes amounts paid for tin plate during the year regardless of whether such tin plate entered into the manufacture of the products for which payment was received during that year. In deter-

mining the gain from a cash transaction, the cost of goods sold must be deducted. *Doyle* v. *Mitchell Brothers Co.*, 247 U. S. 179. This was further recognized by this Court in the cases of *United States* v. *Anderson, supra,* and *American National Co.* v. *United States, supra,* wherein this Court held that the income of manufacturing and mercantile corporations could not be properly computed on the cash basis.

The case of *Doyle* v. *Mitchell Brothers Co., supra,* arose under the Corporation Excise Tax Act of August 5, 1909, which provided for the return of income on a cash receipts and disbursements basis only. The Court there said that the gross income of manufacturing companies "should consist of the difference between the price received for the goods as sold and the cost of such goods as manufactured," the cost to be ascertained by an addition of a charge to the account of goods as manufactured during the year of the sum of the inventory at the beginning of the year and a credit to the account of the sum of the inventory at the end of the year.

On a cash basis moneys spent for materials not used or sold during the year are not ordinary and necessary expenses but are investments in capital items and can not be deducted under the statutory provision any more than could the cost of the factory building. It is, therefore, necessary in computing income on a cash receipts and disbursements

basis to take into account the increase or decrease in inventory during the year.

In any event it is submitted that the judgments herein are fatally defective in that there are no findings either of fact or law that the basis on which respondents kept their accounts and made their returns for the year 1917 did not reflect their true income. Section 13 (d) authorizes a corporation "keeping accounts upon any basis other than that of actual receipts and disbursements" to "make its return upon the basis upon which its accounts are kept" if such basis clearly reflects its income. Respondents having elected to file on the accrual basis on which their accounts were kept, may not now revert to the cash basis and recover $2,719,159.16 in taxes paid on their original returns without establishing that their accrual basis of accounting did not reflect true income. Their right to have their taxes computed on the cash basis depends, not upon the action of the Commissioner, but upon whether the basis upon which their books of account were kept and their income returned correctly reflects true income.

Section 13 (d) clearly does not give the Commissioner the arbitrary right to reject a return filed upon the basis upon which a taxpayer's accounts are kept. He may so reject a return only where the basis used does not reflect true income. Conversely a taxpayer would not be entitled to have taxes, returned upon the basis upon which its books of ac-

count are kept, computed on the cash receipts and disbursements basis unless that basis did not in fact reflect its income, and their being no finding that the respondents' accrual basis did not correctly reflect true income, it is submitted that the findings of the District Court are insufficient to support the judgments.

The Circuit Court of Appeals in its opinion (R. 262) assumed that the District Court had made such finding. This assumption, however, does not supply this defect. In fact, respondents expressly disclaimed any intent of having the lower court pass upon this issue, their contention being that the Commissioner's action controlled rather than the fact as to whether the basis upon which respondents kept their accounts reflected their true net income. (R. 51, 52.)

CONCLUSION

It clearly appears from this record that neither the returns as made by these corporations nor the computation used by the courts below in determining the net income clearly reflects the true net income of these respondents for the year 1917. The fundamental requirement of the statute is that, whatever basis of accounting be used, the true income must be disclosed by the return. In this fundamental particular, the courts below have committed error and permitted these respondents to pay a tax based not upon their actual income but upon an amount artificially produced and erroneously

called their income. They have done this by treating the so-called "inventory constant account" as a real liability reflecting a part of the cost of goods sold,whereas in fact it represents no existing obligation of the corporation. They have said that the creation of a contingent reserve and the treatment of such a reserve as a real liability constitutes a system of accounting and thus have permitted more than $11,000,000 of admitted income to escape taxation in this year. It, therefore, is respectfully submitted that writs of certiorari should be issued.

CHARLES E. HUGHES, Jr.,
Solicitor General.
MABEL WALKER WILLEBRANDT,
Assistant Attorney General.
MILLAR E. MCGILCHRIST,
Special Assistant to the Attorney General.

JUNE, 1929.



APPENDIX

United States District Court, Southern District of New York

AMERICAN CAN COMPANY, PLAINTIFF
against
FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE of the United States for the Second District of New York, defendant

MISSOURI CAN COMPANY, PLAINTIFF
against
FRANK K. BOWERS, COLLECTOR, ETC., DEFENDANT

AMERICAN CAN COMPANY OF MASSACHUSETTS, plaintiff
against
FRANK K. BOWERS, COLLECTOR, ETC., DEFENDANT

AMERICAN CAN COMPANY OF UTAH, PLAINTIFF
against
FRANK K. BOWERS, COLLECTOR, ETC., DEFENDANT

OPINION

(October 26, 1928)

GODDARD, *District Judge:*

These four actions were brought by the American Can Company, a New Jersey corporation, and

three of its subsidiaries, Missouri Can Company, American Can Company of Massachusetts, and American Can Company of Utah, to recover amounts which they paid on March 15, 1924, as Federal income and excess-profits taxes for the calendar year 1917 with interest from the date of payment. These amounts were paid under protest as a result of additional assessments made in accordance with letters of the Commissioner of Internal Revenue to the plaintiffs, dated March 7, 1921. The amounts claimed by the various plaintiffs are as follows:

American Can Company, $3,874,911.37, with interest at the rate of 6% per annum from March 15, 1924;

Missouri Can Company, $11,489.53, with interest at the rate of 6% per annum from March 15, 1924;

American Can Company of Massachusetts, $13,057.83, with interest at the rate of 6% per annum from March 15, 1924; and

American Can Company of Utah, $3,477.54, with interest at the rate of 6% per annum from March 15, 1924.

Upon stipulation of counsel the four actions were tried together before a jury of one and after all the testimony had been presented, both sides moved for the direction of verdicts.

On March 29, 1918, the returns for companies were filed, under section 13 (d) of the Revenue Act of 1917, showing a consolidated net income of $17,944,400.46 (including $60,010.50 as dividends). After an audit by the Commissioner of Internal Revenue, their income was increased by $1,283,721.37 so that it amounted to $19,278,121.03, and the tax paid. Later, a reaudit was made by the Com-

missioner and as a result he redetermined their income and by his communications to them on March 7, 1921, increased their taxable net income from $19,278,121.03 to $24,949,668.51 (including $60,010.50 as dividends).

The American Can Company and its subsidiaries were manufacturers of cans and other containers made largely from tin plate, and it was necessary for them to maintain a supply of tin plate so as to fill their orders promptly. In 1916, tin plate cost them $3.80 per base box. Some of this they carried over into 1917 and they received further shipments of it at the rate of $3.60 per base box under previous contracts. In the early part of 1917, the price had risen sharply in price and it sold at $7 per base box, and the plaintiffs charged their customers with the tin plate consumed in the manufacture of their finished product at the current market price of $7 per base box of tin plate at the time of the manufacture, irrespective of the price paid for it, so that upon all of such sales they realized an inventory profit of $3.40 per base box during that year besides their normal manufacturing profit. This profit was not reported as income in their returns, the plaintiffs taking the position that this price of $7 per base box was abnormally high because of war conditions and that when that temporary condition was over, prices would drop sooner or later to a more normal level and that as tin plate was the basic material for making cans and containers, it was necessary for them to carry large stocks of it to meet promptly the requirements of customers for their manufactured products; and that to value their stock of tin plate at the current high cost or market under such a situa-

tion was unsound; and that to avoid risk of overstating their incomes and overvaluing their assets they accordingly established an "Inventory Constant Account" and carried their normal stock of tin plate at a constant figure.

This "Inventory Constant Account" was created by certain journal entries. In the instance of the American Can Company—a journal entry was made on January 31, 1917, debiting an account designated "cost ledger" and crediting an account called "inventory write-up" in the sum of $5,403,905.79. A further journal entry was made on the same date debiting various "finished products" accounts and crediting "inventory write-up" in the sum of $647,572.26. These entries, although made on January 31, 1917, were effective as of January 1, 1917. The effect thereof was to increase the value of the opening inventory, in the case of the first journal entry, of inventory of raw materials and goods in process, and in the case of the second journal entry, of inventory of finished products. Part of this "write-up" to the extent of $4,722,000 was transferred to a reserve account called "Inventory Constant." This was done by a journal entry debiting the account called "Inventory write-up" and crediting the account called "Inventory Constant" in the sum of $4,722,000. Mr. Green, the Treasurer of the American Can Company, testified:

> Our inventories were written up on the 1st of January on the $7.00 basis for tin plate, and our operations were charged at that price right straight through the year, and all of the operations and the accounts on our general ledgers were carried at that

figure and the profit and loss and the inventory at the close of the year from a profit and loss standpoint was figured on the same basis. Now that had the effect of decreasing the profits for 1917 to the extent of the constant * * *

The tin plate constant account was set up on our books as applying against the inventory. At the close of 1917, when the balance sheet of the company was made, the $4,722,000 was deducted from the inventory as reported on the high basis, and on that basis the difference between the assets and the liabilities of the company, representing the difference in the surplus, agreed with the profit and loss as figured from a profit and loss standpoint.

* * * * *

Q. So that that was an increase in cost that was not actually sustained by the company, and had the effect of reducing income, did it not? A. It did.

Entries and "write-ups" of like nature were made by the several plaintiff companies, the total amount being $5,671,500. The Commissioner of Internal Revenue ruled that this "Inventory Constant Account" could not be included in the cost of the merchandise sold when deducting the cost from the selling price in computing income, and his reasons in his letter of March 7, 1921, to the American Can Company relative to its item of $4,722,000 are characteristic of those stated to the several plaintiffs respecting similar items in their returns, and are—

(a) This item represents a charge to costs of raw material put in process over the actual cost at which same was inventoried at December 31, 1916. The credit was placed to "Inventory Constant" account. The entry was made in anticipation of a drop in the market at some future date, when a loss would occur on account of high priced inventories at hand.

For income tax purposes, all income must be returned in the year in which realized and if the market should slump at a future date, the loss would be taken in the year in which realized.

The entry referred to above would result in an elimination of profits realized through rise in market values, and therefore, has been disallowed.

It is the taxes which were assessed upon these increases in the respective incomes resulting from the disallowance of this item by the Commissioner, which the plaintiffs now seek to recover after paying it under protest.

The plaintiffs kept their books on an accrual basis of accounting as distinguished from a basis of cash received and disbursed, and filed their returns on such basis for 1917 and all previous years; also 1918. The letters of the Commissioner contain no specific rejection of the returns filed by the plaintiffs or of the accrual basis on which they were made, and the plaintiffs filed no returns for 1917 on the cash basis. The plaintiffs contend that the action of the Commissioner in disallowing this item constituted a rejection of the basis upon which their books were kept and their returns filed, and that consequently

he had no power to redetermine their incomes or to assess taxes upon any basis other than the basis of actual receipts and disbursements. The defendant insists that there was no rejection of the basis on which the returns were filed and that the Commissioner merely disallowed an improper deduction. Statements prepared by the plaintiffs and received in evidence during the trial show that their incomes for 1917, on the basis of actual receipts and disbursements, aggregated $13,231,054.52 (including $60,010.50 as dividends).

Although the record contains quite an array of figures, the real question is whether the act of the Commissioner in eliminating the " Inventory Constant Account" is to be regarded as a rejection of the "basis" upon which the plaintiffs filed their returns and upon which their books were kept, thereby entitling them to file returns on a cash basis for the year 1917, with the result that as their returns for 1916 and 1918 were filed on the basis on which their books were kept or an accrual basis, a very substantial amount of income would escape taxation.

The Acts of Congress which imposed and determined the amounts of the Federal income and excess-profits taxes for 1917 are the Revenue Act approved September 8, 1916, and the Revenue Act approved October 3, 1917. These two Acts together constitute the Revenue Act of 1917. The Act of October 3, 1917, continued some of the provisions of the Act of September 8, 1916; amended others and added some new provisions. While the Act of 1917 changed the rates and method of computing taxes, it did not change materially the method of

determining the amount of the income, subject to taxes. The Revenue Act of 1917 prescribes the basis of actual receipts and disbursements generally described as the cash basis for determining the amount of income subject to taxes. However, under section 13 (d) corporations (section 8 (g) similarly applied to individuals) keeping their accounts on a basis other than that of the cash basis were permitted to file their returns on such other basis, provided it truly reflected the income. Section 13 (d) reads as follows:

> A corporation, joint-stock corporation, or association, or insurance company keeping accounts upon any basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect its income, may, subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned.

The plaintiffs filed their returns under this section.

The tin plate, which cost the plaintiffs $3.60 per base box, was at the end of January, 1917, written up in their inventories as of January 1, 1917, on a valuation of $7 per base box; this difference of $3.40 was carried to their "Inventory Constant Account." The result of this was to inflate the valuation of their tin plate, and, although the companies benefited to the extent of $3.40 per base box, it was not accounted for in their return. Reduction

of profits may be effected by artificially appreciating an opening inventory or by depreciating a closing inventory. The scheme adopted by plaintiffs might be described as an indirect method of claiming a depreciation to which they were not entitled irrespective of the basis upon which their books were kept or their returns filed. The basis theory upon which the plaintiffs' books were kept was in the nature of an accrual basis, and this was not disturbed by the Commissioner; he merely disallowed as a deduction an item which was shown on their books. Gain derived from the sale of assets is income. *Doyle* v. *Mitchell,* 247 U. S. 179; *Stratons Independence* v. *Howbert,* 231 U. S. 399.

Plaintiffs concede that the Commissioner has the authority to correct a return filed upon the cash basis, but insist that section 13(d) creates an exception, and that when a return is filed under this section that the return is immune from any adjustment by the Commissioner and that he must either reject it or accept it as it stands; that he has no authority whatsoever to do anything else.

While it is undoubtedly true that the Commissioner must accept the basis upon which the corporation keeps its books and files its return, or in the alternative require it to file on the cash basis, if it is able to do so, and that he can not compel it to change its basis other than to a cash basis, I do not agree that he is without power to audit a return and adjust items in accordance with the basis upon which it is filed or disallow improper deductions or to allow proper deductions and credits which it may appear the taxpayer rightfully should have had. The plaintiffs' contention as to the limitation of the Commissioner's power over a return filed

under section 13(d), it seems to me, can not be correct. If it were so, corporations which were unable to file a return on the cash basis—and it is well known that there are many so situated because of the nature of their business and records—might escape paying taxes. For if the plaintiffs' position is right, such a corporation, when compelled to file under section 13(d) because unable to file on the cash basis, could then file a return under 13(d) which did not reflect its true income, and the Commissioner would have to accept it without corrections, as it follows that if the Commissioner has no authority to correct a return filed under section 13(d) he would lack authority to correct a return filed under such circumstances. The Supreme Court, in *United States* v. *Anderson,* 269 U. S. 422, held that the Commissioner had the authority to correct a return filed by a corporation upon the basis on which it kept its books (section 13(d)) in a case where it was unable to file on the cash basis; therefore, the Court must have regarded the Commissioner as having the power to correct returns filed under Section 13(d) for certainly there is nothing in the statute which gave the Commissioner authority over that particular return that he did not have in respect to all returns filed under section 13(d). Nowhere in the statute is there found a limitation of his power as to such returns. It seems to me that the reasonable construction of 13(d) wherein it provides that the books and return must reflect income, in that the taxable income must be computable from the basis of accounting adopted, not that such a return is immune from adjustments by the Commssioner in accordance with the basis used.

I think that section 13(d) must be read in the light of the other provisions of the Revenue Act, and that the definitions of what is taxable net income under section 12(a) are applicable to all returns, though, of course, all of them may not be applicable to every return. This is the clear inference from the statements of Mr. Justice Sanford on pp. 100, 101, of the Court's opinion in *American National Company* v. *United States,* 274 U. S. 99. If the definitions of what is taxable net income under section 12(a) are not applicable to all returns, there would be much confusion and, moreover, it would mean that the Commissioner and not Congress had the power of defining what was the taxable net income of a corporation filing under section 13(d). In *United States* v. *Anderson* (supra), p. 437, Mr. Justice Stone states:

> While Sec. 12 (a) taken by itself would appear to require the income tax return to be made on the basis of actual receipts and disbursements, it is to be read with section 13(d) which we have quoted and which obviously limits in some respects the operation of section 12(a) by providing in substance that a corporation keeping its books on a basis other than receipts and disbursements may make its return on that basis provided it is one which reflects income.

This would indicate that the exception provided in section 13(d) applied only to the extent of permitting a corporation to file its return on the basis on which its books were kept, but does not exclude the definitions of income defined in section 12(a).

Section 10 levied a tax upon "the total net income * * * received * * * from all sources by every corporation * * * organized in the United States" except those organized and operated exclusively for religious, charitable, educational purposes, and the other expressly exempted under section 11.

12(a) makes no reference to accounts receivable, accounts payable, inventories, for the obvious reason that these are not used when making a return on the cash basis, but it does list the various deductions which were allowed, such as ordinary and necessary expenses, losses, interest on indebtedness, taxes, and the like.

13(a) which dealt with the filing of returns provided that "the tax shall be computed upon the net income as thus ascertained," namely—by deduction from the gross income received from all sources the various deductions permitted under 12(a).

14(b) provides "When the assessment shall be made as provided for in this title, the returns, together with any corrections thereof which may have been made by the Commissioner, shall be filed * * *."

From the above it would appear that the standard of what is income "from all sources by every corporation" does not change, although the basis of keeping their books and filing their returns may differ; some adopting the method or basis of accounting on cash received and cash disbursed; others using a method or a basis of accruing their receipts and disbursements. Section 13(d) recognized that some corporations found it more practical to keep their books on some other basis than that of cash received and disbursed, and permitted them latitude as to the

precise basis which might be used in keeping their books and in filing their return, but it did not grant to them the exceptional power to say what was income and what was not income, as I read the statute. Where a corporation was in a position to do so, it was permitted to elect whether it would file on the cash basis or under 13(d). Having elected, all the items must be accounted for in a manner consistent with such basis, and if the basis adopted does not "clearly reflect its income," the Commissioner may require them to file on the cash basis, if it is possible for them to do so. But if the basis is a fair one, the Commissioner has the authority under the Act to make any such corrections in the items as may be necessary to make them conform on the basis adopted by the taxpayer so as to reflect income as defined for corporations.

In *United States* v. *Anderson* (supra) the accounts were kept and the return was filed on the basis of accruing all their receipts and disbursements and they accrued on their books in 1916 their munitions taxes for 1916 which were taxable and paid in 1917. They made their returns for 1916 and 1917 on the basis of their books except that they deducted their munitions taxes from their income for 1917 instead of 1918. The Supreme Court sustained the ruling of the Commissioner that their munitions taxes should have been deducted from their 1916 income instead of their income for 1917, and his adjustment of their taxes accordingly. The corporations were not able to make their returns on the basis of actual receipts and disbursements, and the Court held that as their accounts were kept on a basis which clearly reflected their incomes, they were required to make their returns on the basis

of their own books, and that the adjustments made by the Commissioner merely had the effect of making their returns accord with their own books of account. Counsel for plaintiffs rely upon this case as supporting the contention that where a corporation has filed its return on the basis upon which it keeps its books under section 13 (d), the Commissioner has no right to amend or correct it, and his only alternative is to require the corporation to file on a cash basis; that only in the event that the corporation is unable to file a return on the cash basis may the Commissioner amend or correct the return. Perhaps the language of Mr. Justice Stone, on pages 437, 438 is susceptible of this inference when standing alone, where he discusses the Treasury Decision 2433 and the right of the Commissioner to require the return to be made on the basis of receipts and disbursements if the return failed to reflect income. But it seems clear conclusion from his entire opinion that the Commissioner has the option of requiring the corporation to file a return on a cash basis if the basis on which the return was filed does not reflect true income. In other words, if the basis upon which the return is filed is not susceptible of properly reflecting income, then the Commissioner may require them to file on the cash basis; but if the accounts are kept and the return filed upon a basis which will reflect income but does not, because of incorrect items, the Commissioner may make such adjustments as to enable him to compute taxable net income in accordance with the corporation's basis or method of accounting. Obviously, the Court did not hold

the view that the Commissioner had no power to amend or correct a return filed under section 13 (d). Plaintiffs' position must be taken then that while the Commissioner had the power to audit or correct returns filed under 13 (d), its use was limited to special instances. However, if the power exists at all, and concededly it does, under no logical theory or construction of the statute is there support for the idea that the Commissioner's authority was thus confined. He either had the power over all returns filed under 13 (d), or he had power over none of them. The statute permits no middle ground.

The plaintiffs urge that the effect of the words of section 13 (d) "the tax shall be computed upon its income *as so returned*" was to substitute in a case like the one at bar for the purpose of computing the tax the income *as returned* by it instead of its income ascertained as prescribed by section 12(a). And further, that it is the *amount* of the income and not the basis which "as so returned" applies to so that the Commissioner must accept the amount, otherwise he rejects the basis. I think the words "as so returned" refer to the basis for the reasons discussed above, and again in the *Anderson* case, supra, the tax there was not computed on the amount "as returned" but upon the income "as so returned" on their basis after the Commissioner of Internal Revenue had disallowed a deduction claimed in the return.

Counsel for plaintiffs also contend that aside from any question with respect to the powers of the Commissioner under the Revenue Act of 1917, Congress had no power under the 16th Amendment

of the Federal Constitution to levy taxes upon income which had accrued but was not actually received by the taxpayer, so that regardless of any attempt on the part of Congress to clothe him with this authority, he had no power to redetermine the income of the plaintiffs upon any basis other than the basis of actual receipts and disbursements. This contention seems to me to be answered by a reference to the decision and the opinion in the *Anderson* case, supra, where it was pointed out that true income is to be determined by deducting from gross income during the year the total costs and expenses attributable to the production of that income during the year. This is the essence of accrual basis of accounting.

Moreover, in *Brushaber* v. *Pacific R. R.*, 240 U. S. 1, it was held that it was not the 16th Amendment which conferred upon Congress the general power to impose tax upon income, which Congress already had, but that the purpose of the 16th Amendment was to relieve Congress in imposing income taxes in so far as they might be held to be direct taxes from the burden of apportioning such taxes according to population. See also *Bowers* v. *Kerbaugh-Empire,* 271 U. S. 170; *Eisner* v. *Macomber,* 252 U. S. 189.

My conclusion is not in accord with Judge Bodine's decision in *American Can Company* v. *United States,* 20 Fed. (2d) 970, but it is consistent with that of Judge Westerhaven in *Aluminum Castings Co.* v. *Routzahn,* 24 Fed. (2d) 230, where a corporation had filed its return for 1917 under section 13 (d) and the Court sustained the right of the

Commissioner to correct it so as to properly compute the tax due on the basis upon which the return had been filed by deducting from the 1917 return $150,000 paid for munitions taxes in 1917 but which had accrued in 1916.

Accordingly the jury is directed to render verdicts in favor of the defendant.

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Nos. 128, 129, 130

In the Supreme Court of the United States

OCTOBER TERM, 1929

THE UNITED STATES, PETITIONER
v.
AMERICAN CAN COMPANY

THE UNITED STATES, PETITIONER
v.
MISSOURI CAN COMPANY

THE UNITED STATES, PETITIONER
v.
DETROIT CAN COMPANY

ON WRITS OR CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES

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In the Supreme Court of the United States

OCTOBER TERM, 1929

No. 128

THE UNITED STATES, PETITIONER

v.

AMERICAN CAN COMPANY

No. 129

THE UNITED STATES, PETITIONER

v.

MISSOURI CAN COMPANY

No. 130

THE UNITED STATES, PETITIONER

v.

DETROIT CAN COMPANY

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the District Court for the District of New Jersey (R. 78–81) is reported in 20 F. (2d) 970. The opinion of the United States Circuit

Court of Appeals (R. 133–135) is reported in 31 F. (2d) 730.

JURISDICTION

The judgments of the United States Circuit Court of Appeals (R. 136–137) were entered March 5, 1929. Petitions for certiorari to review the judgments were filed June 4, 1929, and granted by this Court on October 14, 1929. (R. 137–138.) The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the correction by the Commissioner of Internal Revenue of the valuation of the inventories of tin plate in respondents' returns made on the accrual basis constituted such a rejection of the basis on which respondents' accounts were kept as to render it necessary under Section 13 (d) of the Revenue Act of 1916 to compute their income on the basis of cash receipts and disbursements.

2. Assuming that the Commissioner in changing the valuation of respondents' inventories has rejected respondents' accrual basis of accounting, does such a rejection made by the Commissioner herein in determining that an additional assessment was due for the year 1917 entitle respondents to a recovery of taxes paid on their returns filed on the accrual basis in the absence of a finding that such accrual basis did not reflect their true income?

3. Assuming that, because of the action of the Commissioner, respondents are entitled to have their income computed on the basis of cash receipts and disbursements, can their income be correctly computed on such basis without the use of inventories?

STATUTES AND TREASURY DECISION INVOLVED

The pertinent portion of the Revenue Act of 1916, c. 463, 39 Stat. 756, 771, reads:

> SEC. 13. (a) The tax shall be computed upon the net income, as thus ascertained, * * *;
>
> * * * * *
>
> (d) A corporation, joint-stock company or association, or insurance company, keeping accounts upon any basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect its income, may, subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned;
>
> * * * * *

The pertinent portion of the Revenue Act of 1917, c. 63, 40 Stat. 300, 305, reads:

> SEC. 206. That for the purposes of this title the net income of a corporation shall be ascertained and returned * * * (c) for the taxable year upon the same basis and

in the same manner as provided in Title I of the Act entitled "An Act to increase the revenue, and for other purposes," approved September eighth, nineteen hundred and sixteen, as amended by this Act * * *.

Treasury Decision No. 2609 promulgated December 19, 1917:

(1) For the purposes of income and excess-profits tax returns, inventories of merchandise, etc., and of securities will be subject to the following rules:

A. Inventories of supplies, raw materials, work in process of production, and unsold merchandise must be taken either (a) at cost or (b) at cost or market price, whichever is lower, provided that the method adopted must be adhered to in subsequent years, unless another be authorized by the Commissioner of Internal Revenue.

* * * * *

C. Gain or loss resulting from the sale or disposition of assets inventoried as above must be computed as the difference between the inventory value and the price or value at which sold or disposed of.

(2) In all other cases inventories must be taken at cost or at value as of March 1, 1913, as the case may be.

STATEMENT

The American Can Company and its subsidiaries, Missouri Can Company and Detroit Can Company, respondents herein, were during 1917 engaged in the business of manufacturing and sell-

ing cans and other containers. They kept their accounts, made their returns, and paid their income and excess-profits taxes for the year 1917 and previous years upon the accrual basis. (R. 2, 87, 97, 107, 116, 126.) Additional assessments were thereafter made against the parent company for 1917 (R. 3), and were paid to the then collector, William H. Edwards, who had collected the original assessments. Thereafter a final audit resulted in further additional assessments for 1917, which were paid to another collector and are involved, not in the instant cases, but in certain other cases hereinafter mentioned. (R. 5.)

Respondents, in the conduct of their business, were required to keep on hand large stocks of tin plate, which was the most important material used by them. (R. 98, 116.) The market price of tin plate rose sharply in the early part of 1917 from $3.60 per base box to $7. Respondents took advantage of this sharp increase in value of stocks on hand by writing up as of January 1, 1917, to $7 per base box, their opening inventories of tin plate, which had cost them but $3.60 per box, and transferring so much of the inventory write-up as was calculated to represent respondents' normal stocks of tin plate to the so-called "inventory constant" accounts set up for the first time in that year.

(The above facts showing the manner in which respondents' books of account reflected this write-up of tin plate in inventory transfer to their "inventory constant" accounts, and the reasons there-

for, are not included in the findings made by the District Court, but are supported by uncontradicted evidence in the record (R. 28, 48, 49) which has been adopted by the Circuit Court of Appeals in its opinion (R. 133) as proved facts.)

This bookkeeping entry had the effect of increasing the cost of goods sold as returned by the respondents and resulted in an understatement of net income to the extent of the amounts credited to their respective "inventory constant" accounts. The net income of the American Can Company was thus understated by $4,722,500 (R. 7), the net income of the Missouri Can Company by $168,500 (R. 7), and the net income of the Detroit Can Company by $70,000. (R. 8.)

The Commissioner of Internal Revenue eliminated this artificial inflation of the cost of goods sold (R. 7–8), increased respondents' net income by the amounts in the "inventory constant" accounts, and made further additional assessments, as follows: American Can Company, $3,383,481.46 (R. 4); Missouri Can Company, $10,110 (R. 98); Detroit Can Company, $4,200. (R. 117.) Respondents filed claims to abate such further additional assessments and filed claims for refund of so much of the taxes theretofore paid as exceeded what they contended was their true tax liability computed on the cash receipts and disbursements basis. The grounds set forth in the claims, which are also the grounds upon which these suits are based, were that the Commissioner, in correcting the valuation of inventories used in the computation of the cost of goods sold,

rejected the basis upon which their accounts were kept and their returns filed, and that as the result of the action of the Commissioner they became entitled, under the provisions of Section 13(d) of the Revenue Act of 1916, to have their income computed on the cash receipts and disbursements basis, and that on such basis respondents' tax liability was not only less than that computed by the Commissioner but was less by $2,719,159.16 than the taxes paid by them on their returns as filed. (R. 79–80.)

The respondents instituted actions against the United States in the District Court for the District of New Jersey under Section 24(20) of the Judicial Code for recovery of the amount of taxes paid to William H. Edwards, former Collector, in excess of what they contended was due. (R. 1, 97, 115.) That court upheld the contentions of the taxpayers that their tax liability should be computed on the cash receipts and disbursements basis. (Exhibit P–7 (R. 59), Exhibit P–8 (R. 65), Exhibit P–9 (R. 66); R. 90, 109, 127.)

Respondents' income on the cash basis adopted by the court was computed without the use of inventories, although it appears that the inventories on hand at the end of the year exceeded in quantity those on hand at the beginning of the year. (R. 69.) The calculation upheld by the court was merely a statement showing the excess of income receipts over income expenditures, each class having no necessary relation to the other. The District

Court has not made findings that the computation of income on the cash basis adopted by it was arrived at without the use of inventories, but this fact was established by the testimony of one of respondents' witnesses (R. 50), and requests for such a finding were made by the Government in each case and were denied. (R. 84, 85, 104–106, 123, 124.)

The cases were tried together in the District Court. Upon the conclusion of the trial there the Government made timely motions for judgments in its favor, which were denied and exceptions were duly taken and allowed. (R. 59.) The Government requested certain express findings of fact in each case, and exceptions were duly taken and allowed to the court's refusal to make the findings requested. (R. 81–85, 102–106, 121–124.) Timely exceptions were also taken and allowed to the findings of fact and conclusions of law as made and filed by the District Court in each case. (R. 91, 109, 127.)

The Circuit Court of Appeals for the Third Circuit affirmed the judgments of the District Court.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred—

I. In holding that the action of the Commissioner in these cases amounted to a rejection of the accrual basis upon which basis the respondents kept their accounts and upon which their returns were made so as to entitle respondents to have their income for the year 1917 computed on the basis of cash receipts and disbursements.

II. In holding that respondents were entitled, as a matter of right, to have their taxes computed on the basis of cash receipts and disbursements in the absence of a finding that the accrual basis, which the Commissioner is said to have rejected, did not in fact reflect their true income.

III. In holding that the respondents' income computed upon a cash receipts and disbursements basis could be correctly determined without showing by the use of inventories the cost of goods sold.

SUMMARY OF ARGUMENT

I. The question whether the correction made by the Commissioner in respondents' returns amounted to a rejection of the basis upon which respondents' accounts were kept involved the application of reasoning to the uncontroverted facts and hence presented a question of law which is reviewable here. If material, the question whether the findings of the amounts of respondents' tax liabilities when computed on the cash basis are supported by evidence is also open to review.

II. The entire dispute arises out of the Commissioner's treatment of the inventory item. Respondents kept their accounts on the accrual basis and treated all items consistently with the exception of the inventory of tin plate. The market price of tin plate rose sharply in the early part of 1917 from $3.60 per base box to $7. Respondents took advantage of this increase in value of stocks on hand by writing up as of January 1, 1917, to $7 per base

box their opening inventories of tin plate which had cost them but $3.60 per box. Since the effect of this was to increase the cost of goods sold as shown on their returns and resulted in an understatement of net income, the Commissioner eliminated this artificial inflation of the cost of goods sold and made additional assessments. The courts below have held that this action of the Commissioner amounted to a rejection by him of the basis upon which respondents' accounts were kept and that the necessary consequence of this rejection was to require that the tax be computed on the cash basis. In a case involving the identical facts the Circuit Court of Appeals for the Second Circuit has held to the contrary. We submit that the decision of the court below puts too narrow a construction upon the statute and sanctions a result which Congress never intended.

The statute authorizes the filing of a return on the basis of the taxpayer's accounts unless such basis does not clearly reflect his income. Respondents kept their accounts and filed their returns on the accrual basis. Even if it should be held that the Commissioner rejected the basis upon which respondents' accounts were kept, we submit that since there is no finding that the basis upon which respondents kept their accounts and filed their returns did not clearly reflect income, the findings do not support the judgment.

III. The findings of the amounts of respondents' net incomes on the cash basis are not supported by

evidence, since it clearly appears that the cost of all tin plate paid for during the year has been charged as an expense against the receipts from finished products in which only a part of such tin plate was used, thus causing respondents' incomes to appear to be less than the actual amounts. Furthermore, in the computations of respondents' incomes on the cash basis no attempt was made to reconcile cash payments in 1917 with accrued liabilities for 1916, with the result that items which were deducted in 1916 when respondents reported on the accrual basis have been again deducted when computing respondents' 1917 income on the cash basis.

ARGUMENT

I

THIS COURT IS NOT PRECLUDED FROM DETERMINING WHETHER THE BASIS UPON WHICH THE RESPONDENTS KEPT THEIR ACCOUNTS CLEARLY REFLECTED THEIR INCOME, OR FROM DETERMINING WHETHER THE RESPONDENTS PROVED WHAT THEIR NET INCOME ON THE CASH BASIS WAS, IF THE QUESTION OF NET INCOME ON THE CASH BASIS BECOMES IMPORTANT

Before discussing the merits of the cases, we wish to consider preliminary questions dealing with the proper scope of the review of the decision of the District Court.

These cases were brought in the District Court under Section 24(20) of the Judicial Code, often referred to as the "Tucker Act."

The petitions allege that the Commissioner objected to the basis upon which respondents "had

valued their inventories of tin plate and determined their net incomes for 1917, and on or about March 7, 1921, the Commissioner of Internal Revenue issued and mailed a letter to the [respondents], of which a copy is hereto attached and made a part hereof marked 'Exhibit A,' in which he stated in substance that the basis on which the [respondents] had valued their inventories of tin plate and determined their net incomes for 1917 was not correct, undertook to revalue their inventories of tin plate, and redetermine their net incomes upon a different basis." (R. 3–4.) This allegation was admitted by the answer. (R. 15.)

Each of the petitions instituting suit in the District Court contains an allegation substantially in the form of the following, which occurs in the suit brought by the American Can Company (R. 5–6):

> On information and belief that the Commissioner of Internal Revenue ruled and determined that the basis upon which the plaintiff and its said subsidiary companies valued their inventories of tin plate and determined their net incomes for 1917 did not clearly reflect their incomes and was not authorized or permitted by the revenue acts applicable to 1917 or the regulations made thereunder, that their incomes for 1917 should not be determined upon the basis upon which they kept their accounts and made their returns and their income and excess-profits taxes for 1917 should not be computed upon their incomes as returned.

As to these allegations, the answer in each case "admits the making of the regulations by the Commissioner of Internal Revenue and his rulings and determinations, but denies that the assessment and collection of the taxes was erroneous and illegal." (R. 15.)

A letter from the Deputy Commissioner to the Can Company (Exhibit A to petition) notified respondents of the assessment of an additional tax which is based solely on an alteration by the Commissioner of the inventory item returned by respondents. No other change was made, and this letter contained no statement to the effect that the Commissioner ruled that the basis upon which respondents kept their accounts did not clearly reflect their income. (R. 7.)

No evidence was adduced by either party of any other or further action taken by the Commissioner.

The District Court, under the heading "Findings of Fact," said (R. 87):

> The Commissioner of Internal Revenue ruled and determined that the basis upon which the plaintiff and its domestic affiliated corporations kept their accounts and made their Federal income and excess profits tax returns for 1917 did not clearly reflect their incomes, that their incomes for 1917 should not be determined upon such basis and that their income and excess profits taxes for 1917 should not be computed upon their incomes as returned.

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It is clear from the record that this "Finding" rests wholly upon the court's view that a change by the Commissioner of a single item in respondents' returns on the accrual basis constituted a rejection of the entire returns and that because of this single item the returns of the respondents and the assessment of their taxes should be made on the basis of cash receipts and disbursements under Section 12.

We submit that this finding is in the nature of a conclusion of law, and that under *United States* v. *Pugh,* 99 U. S. 265; *The Edwin I. Morrison,* 153 U. S. 199, 216; *Sun Mutual Ins. Co.* v. *Ocean Ins. Co.,* 107 U. S. 485, it is open to review in this Court. In the *Pugh case* this Court said (pp. 270–271):

> Confessedly, the court has found all the facts which have been directly established by the evidence. These facts are not evidence, in the sense that evidence means the statements of witnesses or documents produced in court for inspection. They are the results of evidence, and whether they establish the ultimate fact to be reached is, if a question of fact at all, to say the least, in the nature of a question of law. * * *
>
> * * * To avoid misapprehension in the future, we take this opportunity to say that we not only think such a judgment may be reviewed here if the question is properly presented, but that when the rights of the parties depend upon circumstantial facts alone, and there is doubt as to the legal effect of the facts, it is the duty of the court, when requested, to so frame its findings as to put the doubtful

> question into the record. This would not require us on the appeal to decide upon the weight of evidence. That is done in the court below, when the particular fact is found which the evidence tends to prove. The effect of mere evidence stops when the fact it proves is established. After that the question is as to the effect of the fact; and when the evidence in a case has performed its part and brought out all the facts that have been proved, these facts thus established are to be grouped, and their legal effect as a whole determined.

This seems to be the generally accepted rule. In *Bianchi* v. *Vere,* 17 F. (2d) 22, 25, the Circuit Court of Appeals for the First Circuit held that a finding of the Supreme Court of Porto Rico which was based upon inferences drawn from uncontroverted facts "does not have the weight in this court that a finding of fact would have." The Circuit Court of Appeals reached a conclusion contrary to the finding of the court below and, since it was controlling, reversed the judgment. Certiorari was denied by this Court, 274 U. S. 752.

The State courts also recognize the rule that appellate courts may treat as conclusions of law findings which are the result of reasoning and inferences. *Woodward* v. *Carson,* 208 Pa. 144, 145; *Commonwealth T. I. & Tr. Co.* v. *Seltzer,* 227 Pa. 410, 416; *Davies's Estate,* 289 Pa. 579, 584; *Fidelity-Phila. Tr. Co., Ex.* v. *L. V. C. Co., Aplnt.,* 294 Pa.

47, 66; *Blaha* v. *Borgman*, 142 Wis. 43; *Caines* v. *Sawyer*, 248 Mass. 368, 372; *A. T. Stearns Lumber Co.* v. *Howlett*, 260 Mass. 45, 59.

The mere circumstance that this conclusion of law was included by the District Court under the heading "Findings of fact" is in no way determinative. *P. H. & F. M. Roots Co.* v. *United States* (C. C. A. 7th), 17 F. (2d) 337; *Lee Hardware Co.* v. *United States* (C. C. A. 8th), 25 F. (2d) 42; *United States* v. *Tinsley* (C. C. A. 4th), 68 Fed. 433, 434; *O'Reilly* v. *Campbell*, 116 U. S. 418. The findings of fact should not include conclusions of law. *Jackson* v. *United States*, 230 U. S. 1, 18.

Even if the above finding is considered as a finding of fact, it is a finding of ultimate fact. Such a finding would seem to be open to review in this Court to determine whether it is supported by evidence. In *Hathaway & Co.* v. *United States*, 249 U. S. 460, 463, this Court said:

> The Court of Claims found: "There was no unreasonable delay on the part of the Government in approving the contract." This finding, like one of reasonable value, *Talbert* v. *United States*, 155 U. S. 45, 46, is a finding of an ultimate fact by which this court is bound, *unless it appears that the finding was made without supporting evidence* * * *. (Italics ours.)

Although the record in the *Hathaway case* discloses that there was no evidence before the court, two of the cases therein cited (*Cramp* v. *United*

States, 239 U. S. 221; *United States* v. *Clark,* 96 U. S. 37) disclose that in those cases some evidence was brought up which was reviewed here. See also *Collier* v. *United States,* 173 U. S. 79. The Circuit Court of Appeals for the Fifth Circuit also holds the view that the evidence may be reviewed in a suit under the Tucker Act by a party who has made requests for findings of fact and taken exceptions to the court's refusal to make such findings. *Blockton Cahaba Coal Co.* v. *United States,* 24 F. (2d) 180.

We submit, whatever may previously have been the rule here with respect to the review of evidence in Tucker Act cases, that since the enactment of the Jurisdictional Act of February 13, 1925, such a review may be had, as in other cases tried without a jury.

Section 4 of that Act provides that in suits tried in the District Courts wherein they exercise concurrent jurisdiction with the Court of Claims "the judgments shall be subject to review in the circuit courts of appeals like other judgments of the district courts" and that "sections 239 and 240 of the Judicial Code shall apply to such cases in the circuit courts of appeals as to other cases therein."

At the conclusion of the evidence petitioner moved for judgment in each case and duly excepted to its denial (R. 59, 85–86, 106, 125) and assigned the court's rulings as error. (R. 94, 112, 131.) Accordingly the District Court's ruling on peti-

tioner's motion, which was in the nature of a demurrer to the evidence, is open to review under Section 700 R. S., U. S. Code, Title 28, Sec. 875, to determine whether, as a matter of law, the court erred in denying the motion for judgment. The petitioner filed requests for findings and conclusions of law (R. 81, 102, 121) and was allowed exceptions to the findings of fact and conclusions of law adopted by the court. (R. 91, 109, 127.) This was an exception to a ruling of the court in the progress of the trial within the language of Section 700 R. S., which presents the question of law whether there is any evidence to support the findings. *Maryland Casualty Co.* v. *Jones,* 279 U. S. 792; *St. Louis* v. *Western Union Telegraph Co.,* 148 U. S. 92, 96; *Bank of Waterproof* v. *Fidelity & Deposit Co.,* 299 Fed. 478, 482; *Griffin* v. *Thompson,* 10 F. (2d) 127, 128; *Sartoris* v. *Utah Construction Co.,* 21 F. (2d) 1, 2; *Thompson-Starrett Co.* v. *La Belle Iron Works,* 17 F. (2d) 536.

It would seem, therefore, that the foregoing principle, applicable to proceedings in error generally, is equally applicable to the judgments herein against the United States. Unlike cases in the Court of Claims, these cases are heard in the District Courts by a single judge and there was no reason to believe that Congress intended to limit the review of the decision of a single judge in the same manner as the decision of the five judges of the Court of Claims. See *Luckenbach S. S. Co.* v. *United States,* 272 U. S. 533, 537.

Furthermore, even if the rule be that in the ordinary case this Court will not review the evidence for the purpose of ascertaining whether it supports the findings, it should not be applied here, because of an extraordinary situation created by the fact that in the case of *American Can Company* v. *Bowers,* involving the same tax for the same year, and the same taxpayer, the District Court for the Southern District of New York and the Circuit Court of Appeals for the Second Circuit reached a conclusion diametrically opposed to the decisions of the courts below in the instant cases. See *Sanitary Refrigerator Co.* v. *Winters,* 280 U. S. 30, 35–36.

If this Court should decide that the respondents' income should be computed on the cash basis, we contend that the evidence adduced before the District Court was insufficient to sustain the finding as to respondents' true income on the cash basis. For the above reasons, we submit that if this question becomes material, this Court may determine whether the evidence was sufficient.

II

RESPONDENTS' TAXES WERE CORRECTLY ASSESSED BY THE COMMISSIONER ON THE ACCRUAL BASIS, WITH A REVALUATION OF THE INVENTORIES OF TIN PLATE

On the question here involved there is a direct conflict between the Circuit Court of Appeals for the Third Circuit in the instant cases and the Circuit Court of Appeals for the Second Circuit in *American Can Co.* v. *Bowers.* (The opinion of the latter court, filed November 11, 1929, is printed in

an appendix, pp. 36–46, *infra.*) This is not the ordinary case of conflict in principle. It is unusual in that the conflict relates to the tax liability of the same taxpayer for the same tax year arising out of identical facts.

In these cases respondents, who had kept their books and made their returns of income upon the accrual basis for the year 1916 (R. 47–48), also kept their books and made returns of their income on the accrual basis for the year 1917, the year here involved. For this year they reported that their consolidated net income was $17,994,400.46. (R. 68, 87.) In arriving at that figure, respondents valued their inventory of tin plate at a constant figure regardless of changes in cost or market value. (R. 86.) This "inventory constant" was the result of writing up the value of the 1916 closing inventory and tin plate purchased in 1917 at $3.60 per box, to $7 per box. (R. 49.) The Commissioner objected to this method of valuing the tin plate (R. 4, 7), and corrected the inventory item to comply with his regulations (T. D. 2609), which required that they be kept at cost or market value, whichever was lower. This action of the Commissioner had the effect of increasing the consolidated net income to $24,949,688.51. (R. 4.) Respondents assert that the Commissioner thereby rejected the accrual basis, and that a return on the basis of cash receipts and disbursements was therefore required, resulting in a net income, as found by the court, of $13,231,054.52. (R. 66, 89.)

The views of the Government as to the fallacy of the contention of the respondents can not be stated better than in the language of the Circuit Court of Appeals for the Second Circuit in the companion case against the Collector, where it is said:

> The appellee argues that "basis" as used in the statute, includes every process and every method used in determining any factor which affected the amount of the net income stated in the return and requires the consideration of every figure in the return which relates to the net income. Having made their returns, in accordance with such a basis, appellants say there is no occasion for reconciliation of the net profits as per their books with the Federal tax return of 1917. They say that the tax "shall be computed upon the income as so returned" and in construing the basis as used in Sec. 13 (d) that the Commissioner must compute the tax on the income as returned without correction. But the section provides for the computation of the tax upon the income "as so returned" upon the basis upon which the accounts are kept instead of income computed upon the basis of actual receipts and disbursements. The requirement of Section 10 was intended to reflect the true income of the taxpayer. If it does, the return may stand as filed upon the accrual basis. If not, the Commissioner may still, treating the return as on an accrual basis, make corrections on such basis as he would if it were filed upon a cash basis. Here the Commissioner made no change as to the accrual system of accounting. He dis-

allowed the inflation of cost for the tinplate—a sum which did not truly represent its cost—and declined to permit the increase by means of bookkeeping entries. In so doing, he did not change the method of bookkeeping; his act was not an inconsistent treatment of any items on the returns; it was merely a correction of an item incorrectly stated on the same accrual basis. He revalued the inventories in accordance with the truth and his valid regulations. He disregarded the later writeups setting up the "inventory constant" which did not state the truth as to the cost of the tinplate. It must always be borne in mind that in keeping accounts they must truly reflect the costs and disbursements which are either paid or accrued and which may lawfully be deducted. The determination of the value to be placed upon an inventory has no relation to the principle or theory affecting the determination of when income is deemed to be received and when expenses are deemed to be incurred. The valuation used in taking the income or in setting up a reserve against the contingencies of future inventory losses has no reference to the basis of accounting with which the statute concerns itself, and does not amount to a basis of accounting within the purview of Section 13.

The reference in Section 13 (d) to "any basis other than that of actual receipts and disbursements" means an equally basic system of accounting which a taxpayer may employ "unless such other basis does not clearly reflect its income." It has

reference to the two fundamental systems of accounting, generally known as the cash basis and the accrual basis. See *United States* v. *Anderson,* 269 U. S. 422, 440; *Reinecke* v. *Gardner,* 277 U. S. 239, 244. This is shown not only by the language of the Act itself but also by the following excerpt from the report of the Ways and Means Committee of the House (H. Rep. No. 922, 64th Congress, First Session, p. 4), respecting the enactment of Section 13 (d):

> As two systems of bookkeeping are in use in the United States, one based on the cash or receipt basis and the other on the accrual basis, it was deemed advisable to provide in the proposed measure that an individual or corporation may make return of income on either the cash or accrual basis, if the basis selected clearly reflects the income.

The case of *Aluminum Castings Co.* v. *Routzahn* (C. C. A. 6th), 31 F. (2d) 669, now pending in this Court upon writ of certiorari (No. 198, October term, 1929), is to the same effect, the court saying (p. 669) that the return contemplated by Section 13 (d) was the return "ordinarily denominated a return upon the accrual basis."

But while Congress authorized the return of income upon the accrual basis, the statute evinces no purpose to limit the Commissioner's power to correct such returns. The whole purpose of the statute is to levy a tax upon the true net income and all the provisions with respect to returns must be

read in the light of this purpose. In *United States* v. *Mitchell,* 271 U. S. 9, 12, this Court said:

> Notwithstanding the option given taxpayers, it is the purpose of the Act to require returns that clearly reflect taxable income.

In order to effectuate such a purpose, it is necessary that the Commissioner have power to make corrections in all returns irrespective of the basis upon which they are made. Section 14 (a) provides that in cases of erroneous, false, or fraudulent returns the Commissioner shall make a return and Section 14 (b) provides that "the returns, together with any corrections thereof which may have been made by the commissioner, shall be filed in the office of the Commissioner of Internal Revenue * * *." With respect to this section, the Circuit Court of Appeals for the Second Circuit pertinently remarked in the case of *American Can Co.* v. *Bowers, supra:*

> The term "returns" necessarily is generic and embraces all returns whether they be upon a basis of cash or accrual system of bookkeeping.

The result of the decision in the instant case is to deny the Commissioner the right to correct returns on the accrual basis. On the other hand, in *Vang* v. *Lewellyn,* 35 F. (2d) 283, the same court passed on a case involving a change made by the Commissioner in a return on the accrual basis, similar in principle to the one made here, without suggestion

that the change required the computation of the tax on the cash basis. In *United States* v. *Anderson,* 269 U. S. 422, 442–443, the taxpayer was on the accrual basis and the controversy concerned the right of the Commissioner to correct the return by the disallowance of a deduction. His right to correct a return on the accrual basis was assumed without discussion. Other courts have similarly assumed such a right. *Aluminum Castings Co.* v. *Routzahn, supra; Chicago Frog & Switch Co.* v. *United States,* decided by the Court of Claims June 3, 1929, not yet officially reported; *Western Dry Goods Co.* v. *United States,* decided by the District Court for the Western District of Washington July 3, 1929, not yet officially reported. See also *Appeal of Tel-Electric Co.,* 1 B. T. A. 434; *Stanfield* v. *Commissioner,* 8 B. T. A. 787, 823.

If the true income is to be shown for a fixed annual period, it is also necessary that the Commissioner have the power to insist that a taxpayer who voluntarily adopts the accrual basis shall consistently follow that basis. Treasury Decision 2433 provides that under Section 13 (d) it will be permissible to file returns on the accrual basis and contains the following statement:

> This ruling contemplates that the income and authorized deductions shall be computed and accounted for on the same basis and that the *same practice shall be consistently followed year after year.* (Italics ours.)

Parts of this Treasury Decision have received the approval of this Court in *United States* v. *Anderson*, 269 U. S. 422, and *American National Co.* v. *United States*, 274 U. S. 99. See also *W. S. Barstow & Co.* v. *Bowers*, 15 F. (2d) 75, 77; *Robert P. Hyams Coal Co.* v. *United States*, 26 F. (2d) 805, 809.

The theory that if the Commissioner undertakes to correct a return made on the accrual basis, he must then go further and compute the tax on the cash basis is obviously unsound and would not satisfy the requirement that whatever system be adopted it must be consistently followed from year to year. With respect to this the Circuit Court of Appeals for the Second Circuit said in *American Can Co.* v. *Bowers, supra:*

> We find no basis for the argument of the appellants, that the Commissioner's sole authority was to compute income on a cash basis. With the power of correction, as above pointed out, in the Commissioner, he may properly correct and compute income on returns filed on an accrual basis.

The valuation at which inventories are taken obviously has nothing to do with the "basis" of accounting as that term is used in Section 13 (d). While affecting the amount of net income because it enters into the calculation of the cost of goods sold, the valuation placed upon inventories does not involve the basis applied in the treatment of items of income and expenditures. The valuation of in-

ventories thus has no bearing on whether in keeping its accounts a corporation deems its income received and expenses paid only when cash is actually received or disbursed, or when income is accrued and expenses incurred. If one company should value its inventory on the basis of cost or market, whichever is lower, in accordance with the Commissioner's regulation, while another company in the same business should use a different valuation, it would be absurd to require that for this reason the one should be taxed on the accrual basis and the other on the cash basis.

The statute must be given a reasonable construction with the purpose of effectuating the general intent of Congress, even if the literal meaning of the language has to be rejected. *Carbon Steel Co.* v. *Lewellyn,* 251 U. S. 501, 505, 506.

Both the court below and the Circuit Court of Appeals for the Second Circuit in the companion case against the Collector have held that the respondents' method of treating their inventories resulted in distorting their income. The court below held (R. 134) that—

> the reason why the basis used by the plaintiffs in making their return did not reflect their true net income was because of this "inventory constant," $7.00 per box, used in making the inventory of the stock of tin plate, regardless of cost or market value.

Respondents were artificially increasing the cost of finished products by the use of their inventory

constant and it has been held that the returns were erroneous to this extent only. The change made by the Commissioner corrected the only error without disturbing the basic accrual system of accounting so that it is entirely clear that the accrual system as corrected discloses respondents' true net income. Thus the purpose of the statute was carried out, and respondents are not entitled to require that their books be entirely rewritten upon a different basic system. As stated by the Circuit Court of Appeals for the Second Circuit in *American Can Co.* v. *Bowers, supra*:

> The Commissioner has but taxed income in declining to allow this alleged increase of cost. The taxpayer received a gain in the sale of its tinplate, when made into tin cans, to the extent of this increase. It was gain derived from capital and labor or from both combined.

Even if it should be held that the Commissioner rejected the basis upon which respondents' accounts were kept, we submit that the judgments must be reversed because the findings of the trial court are not sufficient to support them. Respondents kept their accounts on the accrual basis and filed their returns on the basis upon which their accounts were kept rather than upon the cash basis, pursuant to Section 13 (d). As the respondents have elected to file their returns and pay their taxes on the basis upon which their accounts were kept in the year in question and previous years, they can not change

to the cash basis, and have a judicial refund made of upwards of $2,719,159, including a substantial part of the taxes paid on their original returns, unless the accrual basis upon which they kept their accounts and filed their returns did not clearly reflect their true income. The burden of establishing all facts essential to the recovery is, of course, upon the respondents. *Botany Mills* v. *United States,* 278 U. S. 282; *United States* v. *Anderson,* 269 U. S. 422; *United States* v. *Mitchell,* 271 U. S. 9. For respondents to recover, it was essential for the trial court to find that the accrual basis upon which respondents' accounts were kept did not "clearly reflect" their income. The finding as to the Commissioner's ruling and determination (R. 87, 108, 126) falls far short of meeting this requirement. Respondents' right to have their taxes computed on the cash basis clearly depends, not upon the action taken by the Commissioner in the premises, but upon whether in fact the basis upon which the books were kept and the income returned clearly reflected respondents' true income. Section 13 (d) does not give the Commissioner the arbitrary right to reject a return filed on the basis upon which a taxpayer's accounts are kept. He may so reject the return only where the basis used does not clearly reflect true income. Likewise, a taxpayer who makes a return upon the basis upon which his accounts are kept may not have his tax computed on the cash basis unless the basis used did

not in fact reflect his income. There being no finding that respondents' accrual basis did not correctly reflect their true income, the findings of the District Court, we submit, are insufficient to support the judgments. *Reinecke* v. *Gardner,* 277 U. S. 239, 245.

III

EVEN IF THE STATUTE REQUIRES THE TAX IN THESE CASES TO BE COMPUTED ON THE CASH BASIS, THE FINDINGS OF THE AMOUNTS OF TAXES DUE ON THE CASH BASIS ARE NOT SUPPORTED BY EVIDENCE

If this Court decides that the statute does not require that respondents' taxes be computed on the cash basis, this point is immaterial.

The trial court made findings (R. 87–90, 108–109, 126–127) to the effect that respondents' incomes on the cash basis were correctly stated in Exhibits P–7 and P–9 (R. 59, 66) and the judgments were based on such findings. The findings were duly excepted to (R. 91, 109, 127), and an exception was also taken to the court's ruling denying petitioner's motion for judgment in each case. (R. 85–86, 106–107, 125.) A brief analysis of the record establishes that the trial court's findings as to respondents' income on the cash basis are not supported by evidence. The evidence shows that the cash computation was arrived at in utter disregard of fundamental principles of Federal income taxation, of the provisions of the statute and regulations, and of elementary business principles.

The so-called net income shown in respondents' cash computation merely represents the excess of

cash receipts over cash disbursements, as shown by the cash books. (R. 37–38; Ex. P–7, R. 59–64; Ex. P–9, R. 66–67.) The computation does not purport to set forth the cost of the goods which when sold produced the income receipts; and the net income shown thereon was arrived at without the use of inventories (R. 50) in violation of provisions of Articles 91 and 92 of Regulations 33, Revised. Thus, among the deductions from gross income there have been included as "expenses" all purchases of tin plate paid for during the year, regardless of whether such tin plate was used during that year. Respondents made heavy purchases of tin plate during 1917, their closing inventories being larger than their opening inventories by some 700,000 base boxes. (Ex. D–1, R. 69.) The computation also includes, as deductions from gross income, bills payable which had accrued in 1916, but which were paid in 1917. These liabilities constituted 1916 deductions to respondents whose returns were filed in that year also on the accrual basis, and by these judgments they are again given the benefit of the same deductions, for concededly no effort was made to reconcile the returns and thus avoid the duplications. (R. 52, 53.)

It is clear from the foregoing that Exhibits P–7 and P–9 fail to reflect respondents' true income either on the cash basis or on any other basis. The computation amounts to no more than the ascertainment of the difference between the amount of

cash actually received and the amount of cash actually paid out in 1917.

True net income of a business, embracing the manufacture and sale of finished products, can not be accurately determined, either on the cash basis or on the accrual basis, by treating receipts from the sale of finished products as gross income without ascertaining the true cost of the goods so sold. *United States* v. *Anderson,* 269 U. S. 422, 440, *supra.* Where more raw material is purchased in any year than is actually used in the manufacture of the finished products sold during that year, it is obvious that the difference between the cost of all and the receipts from the sale of part will be less than the actual profit upon the part sold. It has been shown that respondents bought more tin plate in 1917 than was used during the year and that the calculation of their net income on the cash basis has been made by deducting the cost of all of the tin plate from the proceeds of the sale of the part made into finished products. Thus the income shown by respondents' computations (P–7 and P–9), from which the District Court took the figures used in its findings, is less than respondents' actual income.

It is, of course, impracticable for mercantile and manufacturing corporations to so keep their accounts as to record the cost of the manufacture and sale of each unit of merchandise sold. The same result is accomplished, however, by computing the cost of sales in bulk through the use of inventories.

Thus the computation of the cost of goods sold is made by adding to the purchases made during the year the inventories at the beginning of the year, and deducting therefrom the inventories at the end of the year. That is the method prescribed by the Regulations. (Reg. 33, Revised, Art. 91, 92.) That these Regulations are valid and apply to all returns, whether filed on the cash or the accrual basis, follows from this Court's decisions in the cases of *Doyle* v. *Mitchell Bros. Co.,* 247 U. S. 179, and *Hays* v. *Gauley Mt. Coal Co.,* 247 U. S. 189, where similar regulations under the Corporation Excise Tax Act of 1909, which imposed a tax on the cash basis, were held valid. While these cases involved the sale of capital assets, this Court recognized the necessity of deducting from the gross proceeds of the sale the cost of the assets sold, in order to determine taxable gain. The regulations promulgated by the Commissioner under the 1909 Act, which required the use of inventories by manufacturing companies, were used to illustrate the proper method of determining gross income:

Regulations as to the use of inventories, similar to those promulgated under the 1909 Act, which received the approval of this Court, were promulgated under the 1913 Act, which Act also imposed a tax essentially on the cash basis, and again in Regulations under the 1916 and 1917 Acts. (Regulations 33, Articles 104, 105, 106, 161; Regulations 33, Revised, Articles 91, 92.) These regula-

tions apply to corporations filing on the cash, as well as to those filing on the accrual, basis.

Authority to require inventories whenever necessary was thereafter written into the Revenue Acts, Section 203 of the Revenue Acts of 1918 and 1921; Section 205 of the Revenue Acts of 1924 and 1926; Section 22 (c) of the Revenue Act of 1928. In those sections Congress has recognized that inventories are appropriate in the computation of net income and has not restricted their use to the accrual system. With respect to these regulations, the Circuit Court of Appeals for the Second Circuit said in *American Can Co.* v. *Bowers, supra:*

> Indeed, the appellants have failed to comply with the Departmental Regulation 33 (Revised), Articles 91 and 92, promulgated under the Act of 1917 which, in effect, require manufacturing and mercantile corporations to compute their income tax under the act in question through the use of inventories showing gross income as consisting of the difference between the price received for the goods sold and the cost of such goods as manufactured. Such regulations are valid, whether applied to a cash or accrual basis of return.

In *Chicago Frog & Switch Co.* v. *United States, supra,* the Court of Claims said:

> In ascertaining the income of concerns conducting a business such as that of plaintiff that requires large stocks to be carried, it

was absolutely necessary to have inventories made, and the provisions of the act could not be enforced without them.

CONCLUSION

In view of the foregoing we respectfully submit that the judgments of the court below should be reversed.

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DECEMBER, 1929.

APPENDIX

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

American Can Company, plaintiff-appellant, against Frank K. Bowers, Collector of Internal Revenue of the United States for the Second District of New York, defendant-appellee. American Can Company of Utah, plaintiff-appellant, against Frank K. Bowers, Collector of Internal Revenue of the United States for the Second District of New York, defendant-appellee. American Can Company of Massachusetts, plaintiff-appellant, against Frank K. Bowers, Collector of Internal Revenue of the United States for the Second District of New York, defendant-appellee. Missouri Can Company, plaintiff-appellant, against Frank K. Bowers, Collector of Internal Revenue of the United States for the Second District of New York, defendant-appellee.

Before: MANTON L. HAND, and SWAN, *Circuit Judges.*

Appeal from the District Court for the Southern District of New York. Actions by four plaintiffs to recover additional income and excess-profits taxes paid under duress. Judgments directed for the defendant; plaintiffs appeal. Affirmed.

Simpson, Thacher & Bartlett, Esqs., attorneys for appellants; Philip G. Bartlett, Esq., Graham Sumner, Esq., A. McCalman, Esq., of counsel.

Charles H. Tuttle, Esq., United States Attorney, Thomas J. Crawford, Esq., Special Asst. to the Attorney General; Edward Feldman, Esq., Assistant U. S. Attorney, of counsel.

MANTON, *Circuit Judge:*

The four appellants in these actions seek recovery of additional income and excess-profits taxes paid under duress for the year 1917 (39 St. 756; 40 Stat. 300). During the year 1917 the appellants kept their books and filed returns, as permitted by Sec. 13 (d) of the Revenue Act of 1917, showing a consolidated net income of $17,944,400.46 which included $60,010.50 as dividends. This income was increased, when audit was made by the Commissioner, and upon a reaudit was again increased so as to show a net income of $24,949,668.51, including the dividends.

Appellants are engaged in manufacturing and selling tin cans and other containers. It was necessary to have on hand constantly tin plate for their manufacture. In 1916 they paid $3.60 per box for tin plate. There was a sharp rise in price in the latter part of 1916 and it reached $7.50 in March, 1917. Appellants charged their customers at the rate of $7 per box, taking advantage of the market increase, and it is established that this increase in price of $3.40 per box was added to their usual manufacturing profit. They did not report this additional profit in their return so made. By journal entry, on January 31, 1917, the American Can Company wrote up as its inventory of raw materials and

goods in process by crediting its "inventory write-up" account by $5,403,406.70 and debiting the cost ledger the same amount. By journal entry it increased its inventory of finished products by crediting inventory write-up and debiting various finished products accounts by the same amount. Thus, by these entries, they brought the tin plate inventories from the actual cost of $3.60 per box up to $7. The total inventory write-up of this company amounted to $6,514,479.04, part of which is shown in the profits of the company, but $4,722,500 is claimed to represent the write-up of "normal stocks" and went into a special account set up for the first time in January, 1917, called "Inventory Constant." This account was set up by means of a journal entry whereby inventory write-up was debited and the new "inventory constant" account credited with this sum. Similar bookkeeping entries were made in the books of the other appellants in all involving the sum of $5,671,500. Thus, the book cost of goods was increased and the income understated.

The appellants reported the higher costs rather than the lower costs in their returns. This inflation of cost was disallowed by the Commissioner. It was proved that the appellants took their closing entries in their entirety, inclusive of normal stocks, for the purpose of profit and loss estimates, at cost or market, whichever were lower, and they were unable to establish that they had on hand at the end of 1917 any of the tin plate which had cost them $3.60 per box. The book elimination of this additional income was due to the write-up and the entries in other accounts. The "constant" accounts were liability accounts, and were constituted reserve accounts to take care of inventory losses in

future years. The treatment of the "constant" accounts is similar to the treatment in balance sheets of reserves for depreciation.

Appellants claim that this item does not constitute a part of their true consolidated net income as reported on an accrual basis. They contend that the same is not taxable income under the statute. Section 13 (d) of the act provides:

> A corporation * * * keeping accounts upon any basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect its income, may, subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned.

This act, as amended in part by the 1917 Act, was intended by Congress to extend the income tax as far as possible to all species of income. (*Heiner* v. *Columbia Trust Co.*, 275 U. S. 235; *Irwin* v. *Gavit*, 268 U. S. 161.) The section deals with a system of accounting where the taxpayer's accounts are kept on any basis other than actual receipts and disbursements. The income is presumed to have been received, even though not actually received and expenses incurred, even though not actually disbursed. The cash basis of accounting had theretofore been dealt with by Congress which referred to the actual receipts and disbursements. This new basis or system of accounting refers to other than a cash basis. It is based upon the fundamental principle upon which the corporate accounts are kept. If, when arriving at income, the bookkeeping

system contemplates that receipts and disbursements are deemed received and disbursed when the income accrued and the liabilities are incurred, then the basis of accounting is that of an accrual system, as pointed out by the Supreme Court in *United States* v. *Anderson* (269 U. S. 422). In construing Sec. 13, difficulties were involved in the preparation of income accounts on a strict basis of receipts and disbursements. Because of business complexity, when considering the acts of 1909 and 1913, it became necessary to authorize, by departmental regulation, a method of preparing returns not in terms provided by those statutes. This gave rise to the purpose of the act of 1916. (Secs. 12 (a) and 13 (d).) It was to enable taxpayers to keep their books and make their returns according to scientific accounting principles by charging against income earned during the taxable year, the expenses incurred in and properly attributable to the process of earning the income during that period, and to require the tax return to be made on that basis, if the taxpayer failed or was unable to make the return on a strictly cash received and disbursed basis.

The courts have held that in keeping accounts on an accrual basis, referred to in the statute, it was intended that there may be charged against income earned during the taxable period, the expenses incurred in and properly attributable to the process of earning income during the period. (*United States* v. *Anderson, supra; Aluminum Castings Co.* v. *Routzahn,* 31 Fed. (2d) 669.) Necessarily, net income, for tax purposes, is a conception of the income-tax statute and the amount arrived at is ascertained by deducting from the gross amount of income received by the taxpayer from all sources, the

specified deductions allowed to it by statute. For corporate purposes only, it may well be, on the other hand, that net income may be arrived at by the deduction of entries and accounts which are not permissible for purposes of taxation. (*Weiss* v. *Wiener*, 279 U. S. 333.) The appellee argues that "basis " as used in the statute includes every process and every method used in determining any factor which affected the amount of the net income stated in the return and requires the consideration of every figure in the return which relates to the net income. Having made their returns, in accordance with such a basis, appellants say there is no occasion for reconciliation of the net profits as per their books with the Federal tax return of 1917. They say that the tax " shall be computed upon the income as so returned" and in construing the basis as used in Sec. 13 (d) that the Commissioner must compute the tax on the income as returned without correction. But the section provides for the computation of the tax upon the income "as so returned" upon the basis upon which the accounts are kept instead of income computed upon the basis of actual receipts and disbursements. The requirement of S10 was intended to reflect the true income of the taxpayer. If it does, the return may stand as filed upon the accrual basis. If not, the Commissioner may still, treating the return as on an accrual basis, make corrections on such basis as he would if it were filed upon a cash basis.

Here the Commissioner made no change as to the accrual system of accounting. He disallowed the inflation of cost for the tin plate—a sum which did not truly represent its cost—and declined to permit the increase by means of bookkeeping entries. In

so doing, he did not change the method of bookkeeping; his act was not an inconsistent treatment of any items on the returns; it was merely a correction of an item incorrectly stated on the same accrual basis. He revalued the inventories in accordance with the truth and his valid regulations. He disregarded the later write-ups setting up the "inventory constant" which did not state the truth as to the cost of the tin plate. It must always be borne in mind that in keeping accounts they must truly reflect the costs and disbursements which are either paid or accrued and which may lawfully be deducted. The determination of the value to be placed upon an inventory has no relation to the principle or theory affecting the determination of when income is deemed to be received and when expenses are deemed to be incurred. The valuation used in taking the income or in setting up a reserve against the contingencies of future inventory losses has no reference to the basis of accounting with which the statute concerns itself, and does not amount to a basis of accounting within the purview of S13. The statute necessarily intends to impose a tax upon the true income when the return is on the accrual basis.

But the appellants contend that the Commissioner may not correct a return filed on an accrual basis in taxing income on such basis, but must either accept the return as made or restate the income on the cash basis. This is another way of saying that the computation of income may not be corrected if the return be on an accrual basis, and this is based upon the alleged lack of power on the part of the Commissioner to make correction. In order

to ascertain his profit, the taxpayer necessarily must deduct the actual cost, in the computation, from his sale price. In the departmental practice (Treasury Decision 2609), the Commissioner requires inventories to be taken at cost or market, whichever is lower, and such regulations accord with the best accounting practice and have met with approval in the subsequent revenue acts of 1918, 1921, 1924, 1926, and 1928. (See *United States* v. *Kemp,* 12 Fed. (2d) 7; *Chicago Frog & Switch Co.* v. *United States* (Court of Claims, June 3, 1929).)

The statute (S10) assessed the tax upon the total net income received from all sources by every corporation. Section 11 provides exemptions; S12 prescribes how the total net income shall be computed and authorizes deductions "from the gross amount of * * * income received within the year from all sources," such as ordinary and necessary expenses, losses sustained and charged off within the year, interest paid on indebtedness to the extent therein prescribed, and taxes paid within the year, except income and excess profits taxes. Subdivision (b) of S13 requires that every corporation shall be taxed after rendering a true and accurate return "containing such facts, date, and information as are appropriate and in the opinion of the Commissioner necessary to determine the correctness of the net income returned and to carry out provisions of this title * * *". Section 14 (a) provides that in cases of erroneous, false, and fraudulent returns, the Commissioner shall make a return upon information obtained as provided for, and S14 (b) provides that "the returns, together with any corrections thereof, which may

have been made by the Commissioner, shall be filed in the office of the Commissioner of Internal Revenue." The term "returns" necessarily is generic and embraces all returns whether they be upon a basis of cash or accrual system of bookkeeping. In his examination, the Commissioner was entitled to such information as would give him the entire income from all sources, less the statutory deductions to which the taxpayer was entitled. We find no basis for the argument of the appellants, that the Commissioner's sole authority was to compute income on a cash basis. With the power of correction, as above pointed out, in the Commissioner, he may properly correct and compute income on returns filed on an accrual basis.

It may not be argued that the provisions of S12 (a) which define taxable net income apply only to returns on a cash basis and have no application to returns filed on an accrual basis under S13 (d) and S10 of the 1916 Act as amended by S4 of the 1917 Act which imposes the tax on the total net income received from all sources by every corporation and prescribes a rate of income tax. Section 12 (a) defines how such net income shall be ascertained and refers to net income made taxable by S10. The only definition of net income which is subject to tax, upon any basis, is that defined in S12 (a). Reading these sections together it will be observed that the provisions referring to income received and expenses paid mean received or paid in accordance with the principle upon which the books are kept. Section 12 (a) and S13 (d) must be read together and in so doing the taxing scheme of the statute is plain. (*United States* v. *Anderson,*

269 U. S. 422; *Amer. National Co., etc.,* v. *United States,* 274 U. S. 99.) In the *Anderson case* the Commissioner disallowed as a deduction from the taxpayer's 1917 gross income, computed upon an accrual basis, munitions tax paid in 1917 but which had accrued in 1916. In supporting such action the Supreme Court recognized that the taxes were there computed, not upon the income as returned, but upon the income corrected to accord with the basis upon which the taxpayer's accounts were kept. In *Aluminum Castings Co.* v. *Routzahn, supra,* it was conceded that the books were kept upon an accrual basis and it was pointed out that the Commissioner had the right to eliminate a deduction wrongfully made.

In *American Can Co.* v. *United States,* 31 Fed. 730 (C. C. A. 3), the court took a view of the questions here presented which is contrary to our conclusions. We find ourselves unable to agree with the reasons advanced by that learned court which persuaded them. The appellants' returns did not truthfully state their income due to the bookkeeping entries which covered an increased valuation over the cost of the tin plate and they have failed to bear the burden of establishing the invalidity of the tax which has been assessed. (*Botany Worsted Mills* v. *United States,* 278 U. S. 282; *United States* v. *Mitchell,* 271 U. S. 9.) The Commissioner has but taxed income in declining to allow this alleged increase of cost. The taxpayer received a gain in the sale of its tin plate, when made into tin cans, to the extent of this increase. It was gain derived from capital and labor or from both combined. (*Taft* v. *Bowers,* 278 U. S. 470; *Merchants Loan & Trust*

Co. v. *Smietanka,* 255 U. S. 509; *Doyle* v. *Mitchell Bros.,* 247 U. S. 179.) Indeed, the appellants have failed to comply with the Departmental Regulation 33 (Revised), Articles 91 and 92, promulgated under the Act of 1917, which, in effect, require manufacturing and mercantile corporations to compute their income tax under the act in question through the use of inventories showing gross income as consisting of the difference between the price received for the goods sold and the cost of such goods as manufactured. Such regulations are valid, whether applied to a cash or accrual basis of return. (*Hays* v. *Gauley Mt. Coal Co.,* 247 U. S. 189.)

The court below properly directed a judgment for the defendant in each case.

Judgments affirmed.

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IN THE

Supreme Court of the United States,

OCTOBER TERM, 1929.

THE UNITED STATES,

Petitioner,

v.

AMERICAN CAN COMPANY.

THE UNITED STATES,

Petitioner,

v.

MISSOURI CAN COMPANY.

THE UNITED STATES,

Petitioner,

v.

DETROIT CAN COMPANY.

BRIEF IN OPPOSITION TO PETITION FOR WRITS OF CERTIORARI.



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IN THE

Supreme Court of the United States.

OCTOBER TERM, 1929.

Nos. 128, 129, 130.

THE UNITED STATES,
Petitioner,
vs.
AMERICAN CAN COMPANY.

THE UNITED STATES,
Petitioner,
vs.
MISSOURI CAN COMPANY.

THE UNITED STATES,
Petitioner,
vs.
DETROIT CAN COMPANY.

BRIEF IN OPPOSITION TO PETITION FOR WRITS OF CERTIORARI.

The petition for writs of certiorari does not state correctly the grounds upon which these suits are based and does not state fully the facts which are established by the record.

These suits were brought in the District Court for New Jersey under Paragraph 20 of Section 24 of the Judicial Code,

as amended by the Revenue Acts of 1921 and 1925, to recover income and excess profits taxes for 1917 which the plaintiffs paid in excess of the amounts which were legally payable. They were tried by the Court without a jury.

The petitions of the plaintiffs were filed and served on January 22, 1926 (R. pp. 2, 28, 193, 201, 227, 236), and the answers of the defendant were filed by the United States Attorney on April 28, 1926 (R. pp. 29, 202, 237). The answers admitted most of the allegations of the petitions. The plaintiffs introduced evidence at the trial to establish the allegations which were denied by the answers and the defendant offered no evidence to controvert that introduced by the plaintiffs. The Court handed down a memorandum decision (R. pp. 160-5) and also made special findings of fact and conclusions of law (R. pp. 174-81, 210-14, 246-9). He found all the facts which were admitted by the pleadings and also additional facts which were established by the undisputed evidence.

The only question involved in these suits is with reference to the amounts of the incomes upon which the taxes should be computed. The Revenue Act of 1917 provided in substance that the net income of every taxpayer should be ascertained upon the basis of actual receipts and disbursements, and that the tax should be computed upon the net income "as thus ascertained", except in cases where a taxpayer kept his (or its) accounts and made his (or its) return upon some other basis which clearly reflected his (or its) income and complied with regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, and provided that in such excepted cases the tax should be computed upon his (or its) income "as so returned" (Rev. Act of 1917, Secs. 1, 5, 6, 8(*a*) and 8(*g*) with respect to individuals, and Secs. 10, 12, 13(*a*) and 13(*d*) with respect to corporations).

The plaintiffs kept their accounts and made their returns for 1917 upon a basis which did not clearly reflect their incomes and did not comply with the regulations made by the Commissioner, with the approval of the Secretary of the

Treasury. The Commissioner ruled and determined that the basis used by the plaintiffs did not clearly reflect their incomes and was not authorized or permitted by the Revenue Act or the regulations made thereunder, and that their incomes should not be determined upon such basis. He thereupon redetermined their incomes and reassessed their taxes upon a basis which was different from the basis used by the plaintiffs and also different from the basis of actual receipts and disbursements prescribed in the Revenue Act.

The incomes of the plaintiffs upon the basis of actual receipts and disbursements were less by several million dollars than their incomes as returned by them, and the taxes which were payable upon the basis of actual receipts and disbursements were less by several million dollars than the taxes which the plaintiffs actually paid.

The plaintiffs contend that their taxes should be computed upon the basis of actual receipts and disbursements and that they are entitled to recover the amounts of the taxes which they paid in excess of the amounts which were payable upon that basis.

The defendant contends that the taxes should be computed upon the basis upon which the Commissioner finally redetermined the incomes, and that the plaintiffs are not entitled to recover any amounts of the taxes which they paid.

The question is whether the taxes of the plaintiffs should be computed upon the basis prescribed by Congress in the Revenue Act or upon some other basis prescribed by the Commissioner without any authority from Congress.

There was no dispute at the trial with respect to any question of fact. All the material facts are established by the pleadings or the evidence, and by the findings of the District Court. The decisions of the District Court and the Circuit Court of Appeals (20 Fed. (2nd) 970; 31 Fed. (2nd) 730) are in strict accordance with the Revenue Act and the decisions of this Court, and there is no decision of any Court which holds or indicates that a different result should have been reached.

The provisions of the Revenue Act of 1917 with respect to the determination of the income are entirely different from the provisions of the later Revenue Acts with respect to the determination of the incomes for 1918 and subsequent years. The decision in these suits has no bearing upon, or relation to, the determination of the taxes of these plaintiffs for any year other than 1917, or the determination of the taxes of any other taxpayers for any year, or the future conduct of the Commissioner in the administration of the Revenue Acts. It is of no importance to anybody except the parties to the suits.

The italics used in this brief, including those in quoted passages, are in all cases our own.

Statement of the Case.

The facts which were found by the District Court, including those which are admitted by the pleadings, with references to the pleadings or evidence by which they are supported, are substantially as follows:

The plaintiffs are corporations organized under the laws of New Jersey engaged in the business of manufacturing and selling cans and other containers and having their principal business offices in the City of New York (petitions, pp. 2-3, 193, 227-8, answers, pp. 29, 202, 237).

Prior to March 1921 William H. Edwards was the Collector of Internal Revenue of the United States for the Second District of New York, the district in which the plaintiffs had their principal places of business. Edwards was not in office as such Collector at the time of the commencement of these suits, but since March 1921 Frank K. Bowers was the Collector of Internal Revenue for the Second District of New York (petitions, pp. 3, 193-4, 228, answers, pp. 29, 202, 237).

The plaintiffs and their domestic affiliated corporations *kept their accounts* during 1917 *upon the basis of* accruing their receipts and disbursements, *valuing the normal stocks*

of tin plate carried in their inventories at a constant figure regardless of changes in the cost or market value of tin plate, and valuing the other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased (findings, pp. 174-5, 211-2, 246-7, evidence, pp. 56-8).

The plaintiffs and their domestic affiliated corporations *determined their incomes and made their Federal income and excess profits tax returns for 1917 upon the basis upon which their accounts were kept.* Said returns were filed in March, 1918 with Edwards, the Collector of Internal Revenue for the Second District of New York. The amount of the net income of the American Can Company as so determined and returned was $16,927,404.35 (including $60,010.50 as dividends upon the stock of other domestic corporations). The amount of the net income of the Missouri Can Company as so determined and returned was $253,559.18. The amount of the net income of the Detroit Can Company as so determined and returned was $104,786.64. The amount of the consolidated net income of the plaintiffs and their domestic affiliated corporations as so determined and returned was $17,994,400.46 (including $60,010.50 as dividends upon the stock of other domestic corporations) (findings, pp. 175, 212, 247, evidence, pp. 61, 104, 106, 112, 121).

On or about June 14, 1918 the American Can Company paid and Edwards collected $3,266,499.86 as and for the income taxes for 1917 payable by the American Can Company and the excess profits tax for 1917 payable by the plaintiffs and their domestic affiliated corporations, the Missouri Can Company paid and Edwards collected $15,213.54 as and for the income taxes for 1917 payable by the Missouri Can Company, and the Detroit Can Company paid and Edwards collected $6,287.19 as and for the income taxes for 1917 payable by the Detroit Can Company, in accordance with the returns filed by them respectively. The total amount of the excess profits tax was allocated to and paid by the American Can Company as the parent corporation (findings, pp. 175, 212, 247, evidence, pp. 59-60, 100-2).

After June 14, 1918 and prior to September 21, 1920 the Commissioner of Internal Revenue made assessments against the American Can Company for additional income and excess profits taxes for 1917, aggregating $1,953,480.79. The American Can Company paid and Edwards collected $520,762.54 on or about November 22, 1919 and $1,432,718.25 on or about September 21, 1920 as and for such additional taxes (findings, p. 176, petition, pp. 4-5, answer, p. 29).

Thereafter the *Commissioner of Internal Revenue objected to the basis upon which the plaintiffs and their domestic affiliated corporations had valued their inventories of tin plate and determined their net incomes for 1917,* stated in substance that such basis was not correct, *undertook to revalue their inventories of tin plate and redetermine their net incomes upon a different basis* and made assessments for additional income and excess profits taxes for 1917 aggregating $3,397,791.46 (petitions, pp. 5-6, 195, 229-30, answers, pp. 29, 202,237).

Thereafter the plaintiffs filed with Bowers, as Collector of Internal Revenue, claims for the abatement of said assessments aggregating $3,397,791.46 and also claims for the refund of portions of the taxes which they had paid on June 14, 1918, November 22, 1919 and September 21, 1920. On and after January 26, 1924 the Commissioner disallowed and rejected said claims for abatement and said claims for refund and thereafter the plaintiffs paid to Bowers, as Collector of Internal Revenue, the amounts of the assessments involved in said claims for abatement, with interest, and brought actions against said Bowers in the District Court of the United States for the Southern District of New York to recover back the amounts so paid. Said actions are still pending undetermined (petitions, pp. 6-7, 195-7, 230-1, answers, pp. 29, 202, 237).

The Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, made regulations which provided that all materials carried in inventories should be valued on the basis of (a) cost, or (b) cost or market value,

whichever was lower, with the presumption that the materials in the inventory were those last purchased. *The basis upon which the plaintiffs and their domestic affiliated corporations kept their accounts and made their returns for 1917 was not in accordance with said regulations. The Commissioner ruled and determined that the basis upon which the plaintiffs and their domestic affiliated corporations valued their inventories of tin plate and determined their net incomes for 1917 did not clearly reflect their incomes and was not authorized or permitted by the Revenue Act of 1917 or the regulations made thereunder, that their incomes for 1917 should not be determined upon the basis upon which they kept their accounts and made their returns and that their income and excess profits taxes for 1917 should not be computed upon their incomes as returned* (petitions, pp. 8-9, 198, 232-3, answers, pp. 29, 202, 237).

The Commissioner of Internal Revenue ruled and determined that the basis upon which the plaintiffs and their domestic affiliated corporations kept their accounts and made their income and excess profits tax returns for 1917 did not clearly reflect their incomes, that their incomes for 1917 should not be determined upon such basis and that their income and excess profits taxes for 1917 should not be computed upon their incomes as returned (findings, pp. 176, 212, 247).

The net income of the American Can Company for 1917, determined upon the basis of actual receipts and disbursements prescribed in the Revenue Act of 1917, was $12,754,886.02 ($60,010.50 thereof being dividends upon the stock of other domestic corporations). The net income of the Missouri Can Company for 1917, determined upon such basis was $124,164.87. The net income of the Detroit Can Company for 1917, determined upon such basis was $6,556.48. The consolidated net income of the American Can Company and its domestic affiliated corporations for 1917, determined upon such basis was $13,231,054.52 ($60,010.50 thereof being dividends upon the stock of other domestic corporations) (findings, pp. 176-80, 212-3, 247-8, evidence, pp. 61-8, 75-8, 128-46, 151-2).

The total amount of the Federal income taxes for 1917 payable by the American Can Company upon $12,754,886.02 of net income ($60,010.50 thereof being dividends upon the stock of other domestic corporations) and of the Federal excess profits tax for 1917 payable by the American Can Company and its domestic affiliated corporations upon $13,231,054.52 of consolidated net income ($60,010.50 thereof being dividends upon the stock of other domestic corporations) was $2,514,478.94 (findings, p. 180, evidence, pp. 79, 153).

The amount of the Federal income taxes for 1917 payable by the Missouri Can Company upon $124,164.87 of net income was $7,449.87 (findings, p. 213, evidence, pp. 70, 149).

The amount of the Federal income taxes for 1917 payable by the Detroit Can Company upon $6,556.48 of net income was $393.39 (finding, p. 248, evidence, pp. 70, 150).

No part of the amounts which the plaintiffs, or any of them, had paid or which Edwards collected as and for income taxes for 1917 has been refunded or repaid or credited against any income, war profits or excess profits tax or instalment thereof due or payable by the plaintiffs, or any of them (findings, pp. 180, 214, 248-9, evidence, pp. 70-1).

The conclusions of law found by the District Court were that the plaintiffs had paid and that Edwards, as Collector of Internal Revenue, had collected from the plaintiffs, $2,705,501.71 in the case of the American Can Company, $7,763.65 in the case of the Missouri Can Company, and $5,893.80 in the case of the Detroit Can Company, in excess of the amounts which were legally payable and collectible as and for Federal income and excess profits taxes for 1917, that said amounts were assessed and collected erroneously, illegally, wrongfully and without authority and that the plaintiffs were entitled to judgments for said amounts with interest at the rate of 6% per annum from the dates of payment (pp. 181, 214, 249).

The Revenue Act of 1917.

The Acts of Congress which imposed and determined the amounts of the Federal income and excess profits taxes for 1917 were the Revenue Act approved September 8, 1916 (39 Stat. 756, c. 463), and the Revenue Act approved October 3, 1917 (40 Stat. 300, c. 63). These two Acts, taken together, constitute the Revenue Act of 1917. The Act of October 3, 1917, continued some of the provisions of the Act of September 8, 1916, amended some of its provisions and added some new provisions. The Revenue Acts of 1909, 1913 and 1916 imposed only taxes based upon the amount of the income. The Act of 1917 increased the rates of the income tax and added an excess profits tax based upon the amount of the invested capital and the amount of the income.

There is no doubt that the Revenue Act of 1917 prescribes the basis of actual receipts and disbursements, or the "cash" basis, as the primary basis for determining the amount of the income subject to the income and excess profits taxes. This basis is prescribed and defined in the Act with respect to both individuals and corporations. No other basis for determining income is prescribed or defined in the Act.

The only provisions of the Revenue Act of 1917 which authorize the computation of taxes upon any amounts other than the incomes determined on the cash basis, are Sections 8(*g*) and 13(*d*). The language of these two sections is exactly the same, except that the former applies to individuals and the latter to corporations.

These sections, 8(*g*) and 13(*d*), appeared for the first time in the Revenue Act of 1916. The Revenue Acts of 1909 and 1913 prescribed the cash basis for determining the amount of the income and did not authorize or permit taxpayers to make their returns upon any other basis.

The purpose of these new sections was to enable taxpayers who kept books upon bases other than the cash basis to make returns upon the basis of their books in cases where

the books clearly reflected the income, and to relieve such taxpayers from the burden of redetermining their incomes upon the cash basis. Their purpose was to grant a privilege to the taxpayers rather than to confer additional powers upon the Commissioner.

Section 10(*a*) of Title I of the Revenue Act of 1917 imposes an income tax "upon the total net income *received* * * * by every corporation".

Section 201 of Title II of the Revenue Act of 1917 imposes an excess profits tax upon the income of every corporation, and Section 206 of the same Title provides that "for the purposes of this Title the net income of a corporation shall be *ascertained* and *returned* * * * for the taxable year upon the same basis and in the same manner as provided in Title I" of the Revenue Act of 1917.

Section 12 of Title I of the Revenue Act of 1917, so far as is material, reads as follows:

> "Section 12(*a*). In the case of a corporation, joint-stock company or association, or insurance company, organized in the United States, such net income shall be ascertained by deducting from *the gross amount of its income received within the year* from all sources—
>
> First. All the ordinary and necessary expenses *paid within the year* in the maintenance and operation of its business and properties, including rentals or other payments required to be made as a condition to the continued use or possession of property to which the corporation has not taken or is not taking title, or in which it has no equity.
>
> Second. All losses *actually sustained and charged off within the year* and not compensated by insurance or otherwise, including a reasonable allowance for the exhaustion, wear and tear of property arising out of its use or employment in the business or trade; * * *
>
> Third. The amount of interest *paid within the year* on its indebtedness (except on indebtedness incurred for the purchase of obligations or securities the interest upon which is exempt from taxation as income under this title) to an amount of such indebtedness not in excess

of the sum of (*a*) the entire amount of the paid-up capital stock outstanding at the close of the year, or, if no capital stock, the entire amount of capital employed in the business at the close of the year, and (*b*) one-half of its interest-bearing indebtedness then outstanding. * * *

Fourth. Taxes *paid within the year* imposed by the authority of the United States (except income and excess profits taxes), or of its Territories, or possessions, or any foreign country, or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits."

Section 13(*a*) of Title I provides that "the tax shall be computed upon the net income, *as thus ascertained,* received within each preceding calendar year", etc., obviously referring to the basis for ascertaining net income which is prescribed in Section 12.

Section 13(*b*) of Title I provides that "every corporation * * * subject to the tax herein imposed shall, on or before the first day of March, * * * render a true and accurate return of its annual net income in the manner and form to be prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, and containing such facts, data and information as are appropriate and, in the opinion of the Commissioner, necessary to determine the correctness of the net income returned and to carry out the provisions of this Title I".

Section 13(*d*) of Title I reads as follows:

"(*d*) A corporation, joint-stock company or association, or insurance company, keeping accounts *upon any* basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect *its* income, *may*, subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make *its* return *upon* the basis *upon* which *its* accounts are kept, *in which case,* the tax shall be computed upon *its* income *as so returned.*"

Section 14(*a*) of Title I provides that "all assessments shall be made and the several corporations * * * shall

be notified of the amounts for which they are respectively liable on or before the first day of June of each successive year, and said assessment shall be paid on or before the fifteenth day of June * * * except in cases of refusal or neglect to make a return and in cases of *erroneous,* false or fraudulent returns, in which cases the Commissioner of Internal Revenue *shall,* upon the discovery thereof, at any time within three years after said return is due, *make a return* upon information obtained as provided for in this Title or by existing law; and the assessment made by the Commissioner of Internal Revenue *thereon* shall be paid by such corporation * * * immediately upon notification of the amount of such assessment; * * *"

Section 14(*b*) of Title I provides that "when the assessment shall be made, as provided in this Title, the returns, together with any corrections thereof which may have been made by the Commissioner, shall be filed in the office of the Commissioner of Internal Revenue".

Section 13, including all its subdivisions, appears in the Revenue Act under the heading "Returns", and Section 14, including all its subdivisions, appears in the Revenue Act under the heading "Assessment and Administration". It cannot be presumed that provisions of this character are intended to impose a tax or to affect in any way the substantive provisions of the Act which do impose the tax.

Reinecke v. *Gardner,* 277 U. S. 239, 242-4.

Sections 13(*b*), 14(*a*) and 14(*b*) are purely administrative and they do not affect or qualify in any way the substantive provisions of the Act with respect to the determination of the income and the computation of the tax. These sections do not authorize the Commissioner to make an additional assessment or to make a "correction" of a return unless he makes a new return. The procedure clearly outlined in cases where no return is made or an erroneous return is made, is for the Commissioner to obtain the necessary information and make the return which the Revenue Act *required* the corporation to make, and to make an additional

assessment "thereon". The "corrections" of returns to which reference is made in Section 14(*b*) include only the "corrections" which the Commissioner is authorized to make by making new returns.

It is clear beyond question that in making a return and determining the amount of the income to be stated therein, the Commissioner is bound to follow the substantive provisions of the Act with respect to the determination of the income. There are no provisions in the Act with respect to the determination of the income other than those to which we have already referred.

Section 13(*d*) qualifies Section 12 and Section 13(*a*) to the extent, and only to the extent, that it is inconsistent with them, and it withdraws from Section 12 and Section 13(*a*) those cases, and only those cases, which fall clearly within its terms. Section 12 and 13(*a*) state the general rule. Section 13(*d*) creates an exception. All cases which do not fall clearly within the terms of an exception are necessarily governed by the general rule, and all cases which do not fall clearly within the terms of Section 13(*d*) are necessarily governed by Section 12 and Section 13(*a*).

The only cases which fall within the terms of Section 13(*d*) are cases where a corporation keeps its accounts and makes its return upon a basis which clearly reflects its income and complies with the Regulations, made by the Commissioner, with the approval of the Secretary of the Treasury. If the basis used or the return made does not clearly reflect the income or does not comply with the Regulations, Section 13(*d*) does not apply and the tax should not be computed upon the income "as so returned".

The Revenue Act does not authorize the Commissioner to compute the tax upon anything other than (*a*) the income determined upon the cash basis (Secs. 12 and 13(*a*)), or (*b*) the income "as so returned" (Sec. 13(*d*)). It clearly provides that the income must be determined upon the cash basis except in a case which falls within the terms of Sec. 13(*d*). If a case falls within the terms of Section 13(*d*),

the tax must be computed upon the income as so returned. If a case does not fall within the terms of Section 13(*d*), the tax must be computed upon the cash basis prescribed in Section 12.

The Cases of the Plaintiffs are Governed by Sections 12 and 13(a).

The cases of these plaintiffs do not fall within the terms of Section 13(*d*), because they kept their accounts and made their returns upon a basis which did not clearly reflect their incomes and did not comply with the regulations made by the Commissioner, with the approval of the Secretary of the Treasury. The plaintiffs did not make returns in accordance with Section 13(*d*), and they could not possibly have made returns in accordance with that Section. No corporation could make a return in accordance with Section 13(*d*) unless it kept its accounts upon a basis which clearly reflected its income and complied with the Regulations. It follows necessarily that the cases of these plaintiffs are governed by Sections 12 and 13(*a*).

The mandate of the Revenue Act which applies in these cases is not the provision of Section 13(*d*) that "the tax shall be computed upon its income as so returned", but rather the provision of Section 13(*a*) that "the tax shall be computed upon the net income as thus ascertained", i. e., the net income determined upon the cash basis prescribed in Section 12.

It is obvious that the returns which the plaintiffs made were erroneous and that the Revenue Act *authorized and required* the Commissioner to make new returns for them. Section 14(*a*) provides specifically that in every case of an erroneous return the Commissioner "*shall* * * * make a return" etc. It is also obvious that the returns which the Revenue Act thus *authorized and required* the Commissioner to make could be none other than the returns which the Revenue Act *authorized and required* the plaintiffs to make, and that the only returns which the Revenue Act *authorized or*

required the plaintiffs to make were returns upon the cash basis prescribed in Section 12.

Even in a case where a corporation kept its accounts upon a basis which clearly reflected its income and complied with the regulations, and accordingly had the right to make a return under Section 13(*d*), the Revenue Act did not *require* it to make such a return or authorize the Commissioner to make such a return for the corporation.

The defendant admits that the taxes should be computed upon the cash basis in every case where a corporation kept its accounts or made its return upon a basis which did not clearly reflect its income, and also admits that the returns made by the plaintiffs did not clearly reflect their incomes, but the defendant claims that there is no finding to the effect that the basis used by the plaintiffs did not clearly reflect their incomes (Petition for certiorari, pp. 21-2). The defendant admits and asserts, however, that the basis upon which the plaintiffs valued their inventories was in conflict with the Regulations (Petition for certiorari, p. 14). The defendant does not anywhere contend that the basis upon which the plaintiffs kept their accounts and made their returns did clearly reflect their incomes or that their taxes should be computed upon their incomes "as so returned".

The ultimate question to be determined is whether the taxes of the plaintiffs should be computed upon their incomes "as so returned" or upon their incomes determined upon the cash basis prescribed in Section 12, and the findings of fact show conclusively that the taxes should not be computed upon the incomes "as so returned" and accordingly should be computed upon the incomes determined upon the cash basis.

In the first place the findings show that the basis upon which the plaintiffs kept their accounts and made their returns was not in accordance with the regulations which the Commissioner made, with the approval of the Secretary of the Treasury, with respect to the valuation of inventories. This fact was admitted by the pleadings (R. pp. 8-9, 29, 198, 202, 232, 237), and the Court found that all the facts admitted by the pleadings were true (R. pp. 174, 211, 246). This

fact was also included in the findings which the defendant requested the District Court to make (R. pp. 171, 208, 243). The only purpose of these Regulations was to prescribe the basis or bases for valuing inventories which clearly reflected the income and could be used for tax purposes. The fact that the basis used by the plaintiffs was not in accordance with the regulations shows conclusively that the cases of the plaintiffs did not fall within the terms of Section 13(*d*) and that their taxes should not be computed upon their incomes "as so returned".

In the second place, the findings show that the Commissioner ruled and determined that the basis used by the plaintiffs did not clearly reflect their incomes and was not authorized or permitted by the Revenue Act or the regulations made thereunder, and that their incomes should not be determined upon such basis. This fact was admitted by the pleadings (R. pp. 8-9, 29, 198, 202, 232-3, 237) and also found by the District Court (R. pp. 176, 212, 247). This ruling and determination was in strict accordance with the regulations and the Commissioner could not have made any other ruling or determination without overruling himself and the Secretary of the Treasury. This ruling and determination was made by the Commissioner in the performance of his duties under the Revenue Act, it was within the scope of his authority and was entirely proper and correct. There is no doubt that it was conclusive and binding upon both the plaintiffs and the defendant. The fact that the Commissioner made such ruling and determination shows conclusively that the cases of the plaintiffs did not fall within the terms of Section 13(*d*) and that their taxes should not be computed upon their incomes "as so returned".

The principles which are involved in the interpretation of the findings are well settled by the decisions of this Court.

United States v. *Pugh,* 99 U. S. 265;
Sun Mutual Ins. Co. v. *Ocean Ins. Co.,* 107 U. S. 485;
The Belgenland, 114 U. S. 355;
United States v. *California & Oregon Land Co.,* 148 U. S. 31;
Winton v. *Amos,* 255 U. S. 373.

The defendant seems to be under the impression that these suits and the decisions in favor of the plaintiffs are dependent upon the question whether the action of the Commissioner amounted to a rejection of the basis used by the plaintiffs and that the plaintiffs would not have been entitled to recover if the Commissioner had not taken such action. This impression is wholly erroneous. The plaintiffs would have had the same right to recover even if the Commissioner had taken no action with respect to their returns. The basis of the recovery is the fact that the returns which were made were not in accordance with the Revenue Act and the taxes which were paid were in excess of the taxes which were legally payable.

The defendant argues that the Commissioner did not in fact reject the basis upon which the plaintiffs kept their accounts and made their returns, but that he merely corrected the returns so as to make them conform to that basis (Petition for certiorari, p. 18). The defendant admits that the basis upon which the plaintiffs valued their inventories was in conflict with the Regulations and that the Commissioner adjusted the inventory accounts so as to make them comply with the Regulations (Petition for certiorari, p. 14), but argues that this change in the basis for valuing the inventories did not involve a change in the basis upon which the accounts were kept or the returns were made (Petition for certiorari, pp. 16-18).

We have already pointed out that the question whether the Commissioner rejected the basis used by the plaintiffs is not of controlling importance, but it is obvious that the ruling and determination of the Commissioner to the effect that the basis used by the plaintiffs did not clearly reflect their incomes or comply with the Regulations and that their incomes should not be determined upon such basis amounted to, and was in fact, an unequivocal rejection of the basis. It is hard to see how the Commissioner could have done anything which would have been a more clear rejection of the basis used by the plaintiffs.

Furthermore, the pleadings and the findings establish the fact that the basis used by the Commissioner was different

from the basis used by the plaintiffs. The pleadings admitted that the Commissioner *objected to the basis* upon which the plaintiffs valued their inventories and determined their incomes, and that he undertook to revalue their inventories and redetermine their incomes *upon a different basis* (R. pp. 5-6, 29, 195, 202, 229, 237), and the District Court found that all the facts admitted by the pleadings were true (R. pp. 174, 211, 246).

It is obvious that this change in the basis for valuing the inventories did involve a change in the basis upon which the accounts were kept and the returns were made. The word "basis" as used in Section 13(*d*) cannot mean anything other than a basis or method for determining the income. The basis of actual receipts and disbursements referred to in this Section is the basis or method for determining the income which is prescribed in Section 12. Section 13(*d*) relates only to returns of income, and the word "basis" as used in this Section relates only to the determination of the income.

The basis upon which the accounts are kept or the return is made includes every process and every method which is used in determining any factor which affects the amount of the income. It is not limited to the basic theory or principle of cash or accrual which may underlie the entire accounting system, but it includes every theory and every principle which is involved in any part of the accounting system.

Section 13(*d*) clearly recognized that there was more than one form or kind of an accrual basis, because it recognized that there was more than one form or kind of a basis other than the cash basis. There are no bases other than the cash basis, except those which involve the principle of accruing receipts and disbursements. Section 13(*d*) further recognized that some forms or kinds of an accrual basis would clearly reflect the income and that others would not.

The basis upon which any particular corporation keeps its accounts or makes its return means the particular basis for determining the income which that particular corporation uses in keeping its accounts or making its return. If the corporation uses an accrual basis it means the particular

form or kind of an accrual basis which that particular corporation actually uses.

It is obvious that if inventories are used in connection with any accounting system, the basis upon which, and method by which, the inventories are valued is an essential part of the accounting system. It is also obvious that as there are several different bases or methods for valuing inventories in connection with an accrual basis of accounting for income, there must be several different forms or kinds of an accrual basis. To say that an accrual basis with inventories valued upon one basis is the same as an accrual basis with inventories valued upon a different basis is absurd upon its face. Any change in the basis upon which the inventories are valued must involve a change in the basis upon which the income is determined, and consequently a change in the basis upon which the accounts are kept and the return is made.

The basis for valuing inventories which the plaintiffs used was the basis of valuing the normal stocks of tin plate at a constant figure regardless of cost or market value, and of valuing the other materials carried in the inventories at cost or market value, whichever was lower (R. pp. 56-8, 174-5, 211-2, 246-7). This is admitted by the defendant (Petition for certiorari, p. 14).

On December 19, 1917, the Commissioner, with the approval of the Secretary of the Treasury, issued a Regulation to the effect that inventories "must be taken either (*a*) at cost, or (*b*) at cost or market whichever is lower" (T. D. 2609, Petition for certiorari, p. 11). This was the first regulation which was issued with respect to the valuation of inventories, and it is clear that it prohibited the plaintiffs from making their returns for 1917 upon the basis upon which they kept their accounts. In the latter part of 1919 the Advisory Tax Board, which had been created by the Commissioner for the purpose of passing upon questions arising under the Revenue Acts, considered carefully the nature and effect of several different bases for valuing inventories, including the basis of valuing normal or

base stocks of materials at a constant figure regardless of cost or market value, and ruled that the only bases for valuing inventories which clearly reflected the income and could be used for tax purposes were (a) the basis of cost, and (b) the basis of cost or market value, whichever was lower. (T. B. R. 48, 1 Cum. Bul. 47, T. B. R. 65, 1 Cum. Bul. 51).

In *T. B. R.* 65, the Advisory Tax Board said in part:

> "The question is raised as to whether under the Revenue Acts of 1917 and 1918 the so-called "base stock," "minimum," or "cushion," hereinafter referred to as "base stock," method of taking inventories may be used."
>
> * * * * * *
>
> "According to the base-stock method of taking inventories a manufacturer or dealer values at the same price year after year the minimum quantity of goods which he must have on hand at all times."
>
> * * * * * *
>
> "The Advisory Tax Board is of opinion, therefore, that neither the base stock method of taking inventories nor the moving average method, nor a method based upon the presumption that goods in the inventory are the earliest purchases, is in conformity with the provisions of the Revenue Act of 1917 or of the Revenue Act of 1918, and recommends that no change be made in the present regulations with respect to the method of taking inventories."

The fundamental and controlling facts are that the basis upon which the plaintiffs kept their accounts and made their returns, and the returns which they made, did not clearly reflect their incomes and did not comply with the Regulations. These facts are established conclusively by the record and no amount of argument can change them. It follows necessarily that the cases of these plaintiffs do not fall within the terms of Section 13(*d*), that their taxes should not be computed upon their incomes "as so returned", that the cases of these plaintiffs are governed by Sections 12 and 13(*a*) and that their taxes should be computed upon the cash basis

prescribed in Section 12. The returns which the plaintiffs made were erroneous, and the taxes which the plaintiffs paid were in excess of the taxes which were legally payable.

It is well settled that an erroneous return is not binding upon the taxpayer any more than upon the Government, and that if a taxpayer pays an amount of taxes in excess of the amount which was legally payable he has the right to recover back the excess, regardless of the reason for the overpayment, and regardless of whether it was made voluntarily or under protest or duress.

Revenue Act of 1916, 39 Stat. 756 c. 463, Sec. 14(a);

Revenue Act of 1918, 40 Stat. 1057 c. 18, Sec. 252;

Revenue Act of 1921, 42 Stat. 227 c. 136, Sec. 252;

Revenue Act of 1924, 43 Stat. 253 c. 234, Sec. 281(a), Sec. 1014;

Revenue Act of 1926, 44 Stat. 9 c. 27, Sec. 284, Sec. 1122(c);

Judicial Code, as amended Feb. 24, 1925, Sec. 24, par. 20;

U. S. v. *Hvoslef,* 237 U. S. 1;

Capewell Horseshoe Nail Company v. *Walsh,* 1 Fed. 2nd 818 (D. C. Conn.); 4 Fed. 2nd 991 (C. C. A., 2nd Cir.);

Beatty v. *Heiner,* 10 Fed. 2nd 390 (D. C. Pa.);

Warner v. *Walsh,* 24 Fed. 2nd 449 (D. C. Conn.);

Baker & Taylor Co. v. *U. S.,* 26 Fed. 2nd 187 (C. C. A., 2nd Cir.).

POINT I.

The Circuit Court of Appeals has not decided any question of law which is important or which is not settled by decisions of this Court.

The Circuit Court of Appeals held (1) that the basis used by the plaintiffs did not reflect their true incomes, and (2) that, since the basis used by the plaintiffs did not reflect their true incomes, their taxes should be computed upon the cash basis prescribed in Section 12 (R. pp. 262-3).

The first of these points involves merely the interpretation of the pleadings and the findings in these particular suits. It does not involve any question of law and does not affect any taxes other than those payable by the plaintiffs for 1917.

The second of these points involves merely the interpretation of Sections 12, 13(*a*) and 13(*d*) of the Revenue Act of 1917. It involves a question of law but does not affect any taxes other than those payable by the plaintiffs for 1917. This question of law is not involved in any other case arising under the Revenue Act of 1917 and it could not be involved in any case arising under the Revenue Acts for 1918 and subsequent years. There are no provisions in any of the later Revenue Acts similar to those of Sections 12, 13(*a*) and 13(*d*) of the Revenue Act of 1917.

The Revenue Act of 1918 (40 Stat. 1057, c. 18) established an entirely new scheme for determining the income and this new scheme has been used in all the later Revenue Acts.

Instead of providing that the income should be determined upon the cash basis, except in cases where the taxpayer kept his accounts and made his return upon some other basis which clearly reflected his income and complied with the Regulations, and that in such excepted cases the tax should be computed upon his income as so returned, the Revenue Acts for 1918 and subsequent years provided in substance

that the income should be determined upon the basis upon which the accounts were kept, except in cases where such basis did not clearly reflect the income, and that in such excepted cases the incomes should be determined upon such basis as, in the opinion of the Commissioner, did clearly reflect the income. These later Acts conferred upon the Commissioner the power to determine what basis clearly reflected the income of the taxpayer and to redetermine the income upon that basis. They did not limit the Commissioner to the income determined upon the cash basis or the income "as so returned". Under these later Acts there is no "statutory" basis for determining the income.

Section 233(*a*) of the Revenue Act of 1918 provided that in the case of a corporation the term "gross income" means the gross income as defined in Section 213, with certain exceptions applicable to insurance companies. Section 213 provided that the term "gross income" includes "gains, profits and income derived from * * * trades, businesses, commerce, or sales, or dealings in property, etc.".

Section 234(*a*) provided that in computing the net income of a corporation there shall be allowed as deductions "(*a*) all the ordinary and necessary expenses *paid or incurred* during the taxable year in carrying on any trade or business, etc., (2) all interest *paid or accrued* within the taxable year on its indebtedness, etc., (3) taxes *paid or accrued* within the taxable year, etc." and certain other amounts representing losses, depreciation, amortization, etc.

The last paragraph of Section 200 provided:

> "The term 'paid', for the purposes of the deductions and credits under this title, means 'paid or accrued' or 'paid or incurred', and the terms 'paid or incurred' and 'paid or accrued' shall be construed according to the method of accounting upon the basis of which the net income is computed under Section 212."

Subdivision (*b*) of Section 212, an entirely new and most important provision, was as follows:

> "(*b*) The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) *in accordance*

with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made *upon such basis and in such manner as in the opinion of the Commissioner does clearly reflect the income.*"

The Revenue Acts prior to 1918 made no reference to inventories, but the Revenue Act of 1918 provided in Section 203:

> "That whenever in the opinion of the Commissioner the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer upon such basis as the Commissioner, with the approval of the Secretary, may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income."

The later Revenue Acts contained substantially the same provisions with respect to the determination of the income and the powers of the Commissioner in connection therewith.

Revenue Act of 1921, approved Nov. 23, 1921, 42 Stat. 227 c. 136, Secs. 233(*a*), 213, 234(*a*), 200(4), 212(*b*), 203.

Revenue Act of 1924, approved June 2, 1924, 43 Stat. 253 c. 234, Secs. 233(*a*), 213, 234(*a*), 200(*d*), 212(*b*), 205.

Revenue Act of 1926, approved Feb. 26, 1926, 44 Stat. 9 c. 27, Secs. 233(*a*), 213, 234(*a*), 200(*d*), 212(*b*), 205.

Revenue Act of 1928, approved May 29, 1928, Secs. 21, 22(*a*), 23, 48(*c*), 41, 22(*c*).

The Revenue Acts for 1918 and subsequent years did not prescribe the cash basis or any other basis for determining the income, but they authorized the Commissioner to prescribe the basis upon which the income of each taxpayer should be determined. They did not give to the taxpayer the

privilege of choosing between the cash basis and his book basis, if the latter clearly reflected his income. They did not give to the taxpayer any privilege of any kind with respect to the basis. They provided that the income should be determined in each case upon the basis which clearly reflected the income of the taxpayer, without reference to the basis used by the taxpayer, and they authorized the Commissioner to determine in each case what basis would clearly reflect the income of the taxpayer.

It is obvious that the questions involved in these suits are no longer of any importance or interest to anybody other than the parties to the suits.

Furthermore, the question of law which the Circuit Court of Appeals decided in these suits has already been settled by decisions of this Court.

United States v. *Anderson,* 269 U. S. 422;
Reineke v. *Gardner,* 277 U. S. 239.

While these cases did not involve exactly the question which is involved in the suits at bar, they did involve the interpretation of Sections 12, 13(*a*), and 13(*d*) of the Revenue Act of 1917, and this Court stated in so many words that the income of every corporation should be determined upon the cash basis prescribed in Section 12, except (1) in cases where the corporation kept its accounts and made its return upon an accrual basis which clearly reflected its income and complied with the Regulations, and (2) in cases where the corporation was unable to determine its income and make its return upon the cash basis. The opinions in these cases clearly indicate that if a corporation made an erroneous return the Commissioner had no power to make any return for the corporation other than the one which the Revenue Act *required* the corporation to make, and that if a corporation was able to determine its income and make its return upon the cash basis the Revenue Act did not *require* it to make its return upon any other basis.

The cases of these plaintiffs do not fall within either o these exceptions because (1) the plaintiffs did not keep thei accounts or make their returns upon an accrual basis whic clearly reflected their incomes or complied with the Regula tions, and (2) the plaintiffs were able to determine thei incomes and make their returns upon the cash basis. Th plaintiffs proved at the trial the amounts of their income upon the cash basis and thus proved that the incomes upo which they had paid taxes were in excess of their taxabl incomes, and that the taxes which they paid were in exces of the taxes which were legally payable.

In *United States* v. *Anderson, supra,* the taxpayers kep their accounts upon an accrual basis which clearly reflecte their incomes, but they did not make their returns in accord ance with their books of account. The Commissioner change the returns so as to make them accord with the books an assessed additional taxes which the taxpayers paid. Thi Court held that the taxpayers were not entitled to recove the amounts so paid, because they were not able to determin their incomes or make their returns upon the cash basis an hence were required to make their returns upon the basi of their books. The taxpayers in this case did not clai or prove that their incomes as determined by the Commis sioner were in excess of their incomes upon the cash basi or that the taxes which they had paid were in excess of th taxes which were legally payable.

The situation of these plaintiffs is just the opposite o the situation of the taxpayers in the *Anderson* case. The only alternative open to the taxpayers in the *Anderson* case was to use the basis of their books because (1) they were not able to use the cash basis, and (2) the basis of their books clearly reflected their incomes and complied with the Regulations. The only alternative open to the plaintiffs in the suits at bar was to use the cash basis because (1) they were able to use the cash basis, and (2) the basis of their books did not clearly reflect their incomes or comply with the Regulations.

In *Reinecke* v. *Gardner, supra,* this Court held that the question whether a taxpayer should deduct interest accrued in 1916 but paid in 1917 from his gross income for 1916 or his gross income for 1917 could not be answered, because the record did not show whether the books of the taxpayer reflected his income and did not show on what basis his return was made. The record did show that the taxpayer was carrying on the business of a coal mining corporation and keeping his books upon an accrual basis. This Court said in substance that the taxpayer was required to make his return upon the cash basis unless he kept his books on an accrual basis which accurately reflected his income and actually made his return on that basis (pp. 244-5).

POINT II.

The decision of the Circuit Court of Appeals for the Sixth Circuit in *Aluminum Castings Company* v. *Routzahn* furnishes no basis for the issue of writs of certiorari.

In *Aluminum Castings Company* v. *Routzahn,* 31 Fed. 2nd 699, the corporation kept its accounts and made its return upon an accrual basis, except that it deducted its munitions tax in 1917, the year in which it was paid, instead of 1916, the year in which it accrued. The Commissioner ruled that the munitions tax should be deducted in 1916 instead of 1917 and assessed an additional tax for 1917 which the corporation paid. It was held that the corporation was not entitled to recover the amount so paid. The corporation did not prove the amount of its income upon the cash basis prescribed in Section 12, but claimed that its return was correct because it was made in accordance with the Regulations issued under the Revenue Act of 1913, which permitted returns upon an accrual basis, except for taxes, and permitted the deduction of taxes in the year in which they were paid. All the Court had to

decide was that such Regulations were not valid under the Revenue Act of 1917, as this Court had already decided in *United States* v. *Anderson,* 269 U. S. 422.

As the corporation did not prove the amount of its income upon the cash basis prescribed in Section 12, it was in no position to claim that its taxes should be computed upon that basis. The burden rested upon the corporation to prove that the taxes which it had paid were in excess of the taxes which were legally payable.

United States v. *Anderson,* 269 U. S. 422, 443;
Botany Worsted Mills v. *United States* (Jan. 21, 1929), 49 Sup. Ct. Rep. 129;
Bishoff v. *Commissioner,* 27 Fed. 2nd 91 (C. C. A. 3rd Cir.);
Rouss v. *Bowers,* 30 Fed. 2nd 628 (C. C. A. 2nd Cir.).

The question which the Circuit Court of Appeals decided in the suits at bar was not presented, considered or decided in *Aluminum Castings Company* v. *Routzahn.*

POINT III.

The decision of the District Court for the Southern District of New York in *American Can Company* v. *Bowers* furnishes no basis for the issue of writs of certiorari.

The above proposition is true not only because a conflict between a District Court and a Circuit Court of Appeals furnishes no basis for the issue of a writ of certiorari, but also because there is no conflict upon any question of law between the decision of the District Court in *American Can Company* v. *Bowers* and the decision of the Circuit Court of Appeals in the suits at bar.

In *American Can Company* v. *Bowers* the District Court held that the real question was whether the Commissioner

had rejected the basis upon which the plaintiffs kept their accounts and made their returns, recognizing clearly that if the Commissioner had rejected their basis the taxes of the plaintiffs should be computed upon the cash basis (Petition for certiorari, p. 31). He held further that the Commissioner must accept the basis upon which the plaintiffs kept their accounts and made their returns or, in the alternative, require them to file on the cash basis, and that he could not compel the plaintiffs to change their basis other than to the cash basis, but he held that the Commissioner had power to adjust items in accordance with the basis used by the plaintiffs and that the Commissioner did not disturb the "basic theory" upon which the plaintiffs had kept their accounts but merely disallowed as a deduction an item which was shown on their books (Petition for certiorari, p. 33).

It is clear that if the opinion of the District Court were applied to the record in the suits at bar the result would be in favor of the plaintiffs. The pleadings and the findings in the suits at bar establish conclusively that the basis used by the plaintiffs did not clearly reflect their incomes or comply with the Regulations, that the Commissioner rejected their basis and that the changes made by the Commissioner were not in accordance with their basis. Upon such pleadings and findings the District Court would have held that the taxes of the plaintiffs should be computed upon the cash basis and that the plaintiffs were entitled to recover.

The New York suits were tried by the Court and a jury. The Court made no findings of fact but merely directed verdicts in favor of the defendant. The record made by the pleadings and the evidence is entirely different from the record made by the pleadings and findings in the suits at bar. We are satisfied, however, that the verdicts in the New York suits are contrary to the evidence and contrary to law and that they will be reversed by the Circuit Court of Appeals for the Second Circuit to which appeals have been taken. It is expected that these appeals will be argued next fall.

The opinion of the District Court does not state correctly the contentions which the plaintiffs made, and we contend

that it does not state correctly the questions involved or interpret correctly the provisions of the Revenue Act or the decision of this Court in *United States* v. *Anderson*.

The plaintiffs have never contended that their taxes should be computed upon their incomes "as so returned". They contended in the New York suits that the Commissioner had no power to assess taxes under the Revenue Act of 1917 upon anything other than the income "as so returned" or the income on the cash basis, and that he had no power to redetermine the incomes of the plaintiffs upon any basis other than the cash basis. They admitted that the Commissioner was not bound to accept the returns which they made, but contended that he had no power to make any returns for them other than those which the Revenue Act required them to make, that is, returns upon the cash basis. They contended that the Commissioner had no power to adjust items in accordance with their basis, that the changes which he made were in conflict with their basis, and that he had used a basis which was not authorized by the Revenue Act.

The contentions which the plaintiffs made in the New York suits were not based upon the claim that the Commissioner had rejected their basis or had done anything which would entitle them to file returns upon the cash basis. Their contentions were based throughout upon the Revenue Act and the facts, and the claim that the Commissioner had no power under the Revenue Act to assess the taxes involved in those suits.

The opinion of the District Court deals almost entirely with questions which were not presented, considered or decided in the suits at bar, and there is no point in making any argument about those questions here. The important fact is that there is no conflict upon any question of law between the opinion of the District Court and the opinion of the Circuit Court of Appeals in the suits at bar. The opinion of the District Court is in accord with, and tends to confirm, the decision of the Circuit Court of Appeals upon the only question of law which it decided.

POINT IV.

The decision of this Court in *Doyle* v. *Mitchell Brothers* furnishes no basis for the issue of writs of certiorari.

The statements in the petition with reference to the decision of this Court in *Doyle* v. *Mitchell Brothers*, 247 U. S. 179 are inaccurate and misleading, to say the least (Petition for certiorari, pp. 7, 20). This Court did not hold or say that inventories should be used when the income is determined upon the cash basis, and it did not hold or say anything with respect to the determination of the income of a manufacturing corporation upon the cash basis prescribed in Section 12.

In *Doyle* v. *Mitchell Brothers*, which arose under the Revenue Act of 1909, this Court held that the sale of *capital assets* did not produce income of any kind unless the sale resulted in a profit and that the entire proceeds of the sale of capital assets could not under any circumstances be treated as income, and further, that in order to determine the amount of the profit realized from the sale of the capital assets involved in that case, it was necessary to deduct from the proceeds of the sale the market value of the assets on December 31, 1908, the time when the Revenue Act took effect. The Government contended (1) that the entire proceeds of the sale of the capital assets were income and that the taxpayer had no right to deduct anything therefrom, and (2) that if the taxpayer had the right to deduct anything from the proceeds of the sale it had the right to deduct only the original cost, which was less than the market value on December 31, 1908. In rejecting these contentions, this Court referred to the Regulations which the Commissioner had issued with respect to the determination of the income of manufacturing companies and also the determination of the income realized through the sale of *capital assets*, and said: "In our opinion these Regulations correctly interpret the Act in its applica-

tion to the facts in the present case" (247 U. S. 185-7). This Court did not say that the gross income of manufacturing companies should consist of the difference between the price received for the goods as sold and the cost of such goods as manufactured, such cost to be ascertained by the use of inventories, but it merely said that the Regulations issued by the Commissioner so provided (247 U. S. 185-6). The statement on page 20 of the petition as to what this Court said in the *Doyle* case is not correct. This Court did not adopt or approve the Regulations in so far as they related to the determination of the income of a manufacturing company. It merely adopted and approved them in so far as they related to the determination of the income realized through the sale of *capital assets.*

There is no warrant whatever for the claim that inventories should be used when the income is determined upon the cash basis prescribed in Section 12, for the plain and simple reason that Section 12 makes no reference to inventories. Nor is there any warrant for the claim that the amounts which the Court found to be the incomes of the plaintiffs upon the cash basis were not determined in accordance with Section 12.

Section 12 requires and permits the use of only five factors in determining the amount of the net income (1) the gross amount of the income *received within the year,* (2) the amount of the ordinary and necessary expenses of maintenance and operation *paid within the year,* (3) the amount of the losses actually *sustained and charged off within the year,* (4) the amount of the interest on indebtedness *paid within the year,* and (5) the amount of the taxes *paid within the year.* The net income is ascertained under this Section by deducting the last four factors from the first factor.

The findings and the evidence show separately for each Company, and in the aggregate for all the Companies, the amount of each one of these five factors and that each factor includes the items and only the items which are included in the definition of the factor contained in Section 12. There is no ground for claiming that the amounts given for gross

income fail to include any item which ought to have been included or that the amounts given for the deductions include any item which ought not to have been included. The findings and the evidence show also the amount of the net income of each Company and the consolidated net income of all the Companies upon the cash basis prescribed in Section 12 (R. pp. 176-80, 212-3, 247-8, 61-8, 74-8, 128-46, 151-2).

When the plaintiffs offered in evidence their computation of their incomes upon the cash basis, the defendant asked for an opportunity to examine the books and records of the plaintiffs with a view to checking the correctness of their computation. The plaintiffs did not oppose this application and the Court adjourned the trial for several weeks in order to allow the defendant to check the computation. When the trial was resumed the defendant conceded the figures in the plaintiffs' computation, except for two items which the plaintiffs corrected. There was, accordingly, no dispute about the figures and the defendant is in no position to question the amounts which the Court found to be the incomes of the plaintiffs upon the cash basis (R. pp. 61-9, 74-8, 128-46, 151-2).

It is well settled that when the income is determined upon the cash basis no items should be used or taken into consideration other than items of cash actually received within the year, items of cash actually paid within the year and losses actually sustained within the year.

Maryland Casualty Co. v. *U. S.*, 251 U. S. 342;

U. S. v. *Anderson*, 269 U. S. 422;

United States v. *Mitchell*, 271 U. S. 9;

Mutual Benefit Ins. Co. v. *Herold*, 198 Fed. Rep. 199 (D. C. N. J. 1912); 201 Fed. Rep. 918 (C. C. A. 3rd Cir.);

Connecticut General Life Insurance Co. v. *Eaton*, and *Connecticut Mutual Insurance Co.* v. *Eaton*, 218 Fed. Rep. 188, 206 (D. C. Conn.); affirmed on appeal, 223 Fed. Rep. 1022 (C. C. A. 2nd Cir.);

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U. S. v. *Christine Oil & Gas Co.*, 269 Fed. Rep. 458 (D. C. La.);

Lumber Mutual Fire Insurance Co. v. *Malley*, 256 Fed. Rep. 380 (D. C. Mass.);

Coley v. *Pickering*, 21 Fed. 2nd 247 (Dist. Ct. S. D. Ill.) 1927;

American Can Co. v. *Bowers*, (D. C. N. Y.) (Petition for certiorari, p. 36);

Aluminum Castings Co. v. *Routzahn*, 24 Fed. 2nd 230 (D. C. Ohio); 31 Fed. 2nd 669 (C. C. A. 6th Cir.).

The defendant's real objection to the amounts which the Court found to be the incomes of the plainitffs upon the cash basis prescribed in Section 12 is that they do not reflect the true incomes of the plaintiffs, rather than that they were not determined in accordance with Section 12 of the Revenue Act (Petition for certiorari, pp. 5, 8, 20, 22). The defendant's objection amounts merely to the claim that the cash basis prescribed in Section 12 does not reflect the true income of a manufacturing corporation and, for that reason, should not be used, even though Congress directed that it should be used for the purpose of the taxes for 1917. The defendant is not attempting to apply the Revenue Act but is attempting rather to avoid it.

It is obvious that the defendant is in no position to attack the Revenue Act, and that the Commissioner had no power to assess taxes, except in accordance with the Revenue Act.

POINT V.

The petition for writs of certiorari should be denied.

GRAHAM SUMNER,
JOHN J. TREACY,
Counsel for Plaintiffs-Respondents.

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IN THE

Supreme Court of the United States,

OCTOBER TERM, 1929.

THE UNITED STATES,

Petitioner,

v.

AMERICAN CAN COMPANY.

THE UNITED STATES,

Petitioner,

v.

MISSOURI CAN COMPANY.

THE UNITED STATES,

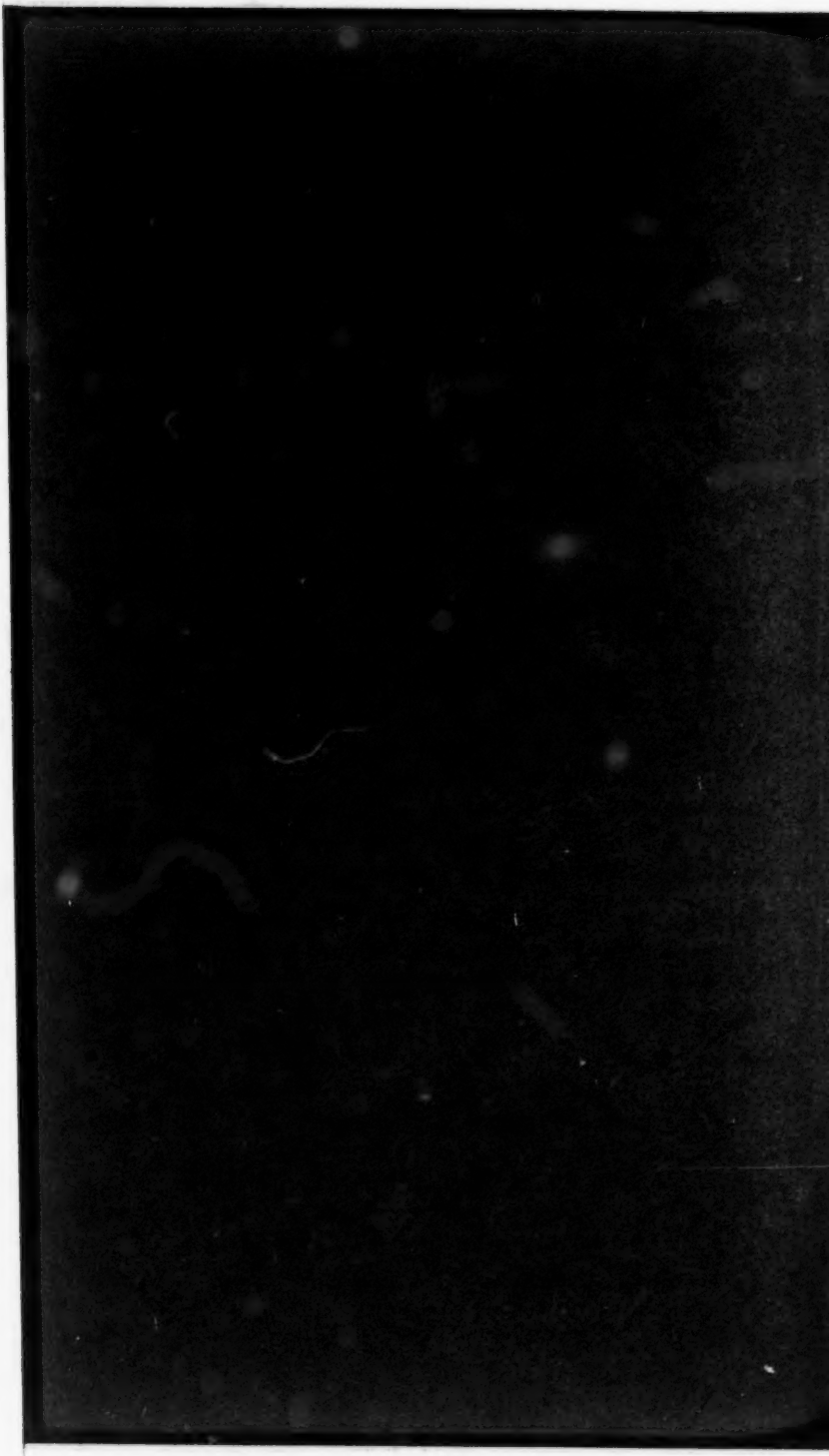
Petitioner,

v.

DETROIT CAN COMPANY.

BRIEF FOR PLAINTIFFS-RESPONDENTS.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.



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IN THE

Supreme Court of the United States,

OCTOBER TERM, 1929.

Nos. 128, 129, 130.

THE UNITED STATES,
Petitioner,

vs.

AMERICAN CAN COMPANY.

THE UNITED STATES,
Petitioner,

vs.

MISSOURI CAN COMPANY.

THE UNITED STATES,
Petitioner,

vs.

DETROIT CAN COMPANY.

BRIEF FOR PLAINTIFFS-RESPONDENTS.

The principal question involved in these cases is whether the net incomes of the plaintiffs, for the purposes of their Federal taxes for 1917, should be determined upon the basis prescribed in Section 12 of the Revenue Act, or upon the basis prescribed in the Regulations made by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury.

The plaintiffs contend that their incomes should be determined upon the basis prescribed in Section 12 of the Revenue Act because:

1. The Revenue Act of 1917 provided that, for the purposes of the Federal taxes, the net income of every corporation should be determined upon the basis prescribed in Section 12 of the Act, except in cases where a corporation kept its accounts and made its return upon some other basis which clearly reflected its income and complied with the Regulations made by the Commissioner with the approval of the Secretary of the Treasury.

2. The plaintiffs did not keep their accounts or make their returns for 1917 upon a basis which clearly reflected their incomes and complied with the Regulations made by the Commissioner with the approval of the Secretary of the Treasury.

The first of these propositions is established by the Revenue Act for 1917 and the decisions of this Court in *United States* v. *Anderson,* 269 U. S. 422, and *Reinecke* v. *Gardner,* 277 U. S. 239. The second of these propositions is established by the pleadings of the parties and the findings of the District Court. Both propositions were sustained by the District Court and the Circuit Court of Appeals.

The Commissioner ruled and determined that the basis upon which the plaintiffs kept their accounts and made their returns for 1917 did not clearly reflect their incomes or comply with the Regulations, but instead of redetermining their incomes upon the basis prescribed in Section 12 of the Revenue Act, he redetermined them upon the basis prescribed in the Regulations. The Commissioner used a basis which was different from the basis used by the plaintiffs and also different from the basis prescribed in Section 12 of the Revenue Act.

The net incomes of the plaintiffs upon the basis prescribed in Section 12 of the Revenue Act were less by several millions

of dollars than their incomes as returned by them, and their incomes as so returned were less by several millions of dollars than their incomes upon the basis prescribed in the Regulations.

The taxes could not be computed upon the basis used by the plaintiffs because that basis did not clearly reflect their incomes and comply with the Regulations.

The taxes could not be computed upon the basis prescribed in the Regulations because the plaintiffs did not keep their accounts or make their returns upon that basis.

The only basis upon which the taxes could be computed was the basis prescribed in Section 12 of the Revenue Act.

The District Court and the Circuit Court of Appeals held that the plaintiffs were entitled to recover the amounts of the taxes which they had paid in excess of the amounts which were payable upon the basis prescribed in Section 12 of the Revenue Act (20 Fed. 2nd 970; 31 Fed. 2nd 730).

These suits were brought against the United States under Paragraph 20 of Section 24 of the Judicial Code, as amended by the Revenue Acts of 1921 and 1925, because the Collector of Internal Revenue to whom the taxes were paid was not in office at the time of the commencement of the suits. They were tried by the District Court without a jury.

The petitions of the plaintiffs were filed and served on January 22, 1926 (R. pp. 1, 14, 97, 101, 115, 119), and the answers of the defendant were filed by the United States Attorney on April 28, 1926 (R. pp. 15, 102, 120). The answers admitted most of the allegations of the petitions. The plaintiffs introduced evidence at the trial to establish the allegations which were denied by the answers and the defendant offered no evidence to controvert that introduced by the plaintiffs. The Court handed down a memorandum decision (R. pp. 78-81) and also made special findings of fact and conclusions of law (R. pp. 86-90, 106-9, 125-9). He found all the facts which were admitted by the pleadings and also additional facts which were established by the undisputed evidence.

Statement of the Case.

The facts which are established by the pleadings and the findings, are substantially as follows:

The plaintiffs are corporations organized under the laws of New Jersey engaged in the business of manufacturing and selling cans and other containers and having their principal business offices in the City of New York (petitions, pp. 1-2, 97, 115, answers, pp. 15, 102, 120).

Prior to March 1921 William H. Edwards was the Collector of Internal Revenue of the United States for the Second District of New York, the district in which the plaintiffs had their principal places of business. Edwards was not in office as such Collector at the time of the commencement of these suits, but since March 1921 Frank K. Bowers was the Collector of Internal Revenue for the Second District of New York (petitions, pp. 2, 97, 115, answers, pp. 15, 102, 120).

The plaintiffs and their domestic affiliated corporations *kept their accounts* during 1917 *upon the basis of* accruing their receipts and disbursements, *valuing the normal stocks of tin plate carried in their inventories at a constant figure regardless of changes in the cost or market value of tin plate,* and valuing the other materials carried in their inventories at cost or market value, whichever was lower, with the presumption that the materials in the inventory were those last purchased (findings, pp. 86, 107, 125-6, evidence, pp. 32-3).

The plaintiffs and their domestic affiliated corporations *determined their incomes and made their Federal income and excess profits tax returns for 1917 upon the basis upon which their accounts were kept.* Said returns were filed in March, 1918 with Edwards, the Collector of Internal Revenue for the Second District of New York. The amount of the net income of the American Can Company *as so determined and returned* was $16,927,404.35 (including $60,010.50 as dividends upon the stock of other domestic corporations). The amount of

the net income of the Missouri Can Company *as so determined and returned* was $253,559.18. The amount of the net income of the Detroit Can Company *as so determined and returned* was $104,786.64. The amount of the consolidated net income of the plaintiffs and their domestic affiliated corporations *as so determined and returned* was $17,994,400.46 (including $60,010.50 as dividends upon the stock of other domestic corporations) (findings, pp. 86, 107, 126, evidence, pp. 35, 59 [104, 106, 112, 121]).

On or about June 14, 1918 the American Can Company paid and Edwards collected $3,266,499.86 as and for the income taxes for 1917 payable by the American Can Company and the excess profits tax for 1917 payable by the plaintiffs and their domestic affiliated corporations, the Missouri Can Company paid and Edwards collected $15,213.54 as and for the income taxes for 1917 payable by the Missouri Can Company, and the Detroit Can Company paid and Edwards collected $6,287.19 as and for the income taxes for 1917 payable by the Detroit Can Company, in accordance with the returns filed by them respectively. The total amount of the excess profits tax was allocated to and paid by the American Can Company as the parent corporation (findings, pp. 86, 107, 126, evidence, pp. 34, 59 [100-2]).

After June 14, 1918 and prior to September 21, 1920 the Commissioner of Internal Revenue made assessments against the American Can Company for additional income and excess profits taxes for 1917, aggregating $1,953,480.79. The American Can Company paid and Edwards collected $520,762.54 on or about November 22, 1919 and $1,432,718.25 on or about September 21, 1920 as and for such additional taxes (findings, p. 86, petition, pp. 2-3, answer, p. 15).

Thereafter the *Commissioner of Internal Revenue objected to the basis upon which the plaintiffs and their domestic affiliated corporations had valued their inventories of tin plate and determined their net incomes for 1917, and revalued their inventories of tin plate and redetermined their net incomes upon a different basis* and made assessments for additional income and excess profits taxes for 1917 aggregat-

ing $3,397,791.46 (petitions, pp. 3-4, 98, 116-7, answers, pp. 15, 102, 120).

Thereafter the plaintiffs filed with Bowers, as Collector of Internal Revenue, claims for the abatement of said assessments aggregating $3,397,791.46 and also claims for the refund of portions of the taxes which they had paid on June 14, 1918, November 22, 1919 and September 21, 1920. On and after January 26, 1924 the Commissioner disallowed and rejected said claims for abatement and said claims for refund and thereafter the plaintiffs paid to Bowers, as Collector of Internal Revenue, the amounts of the assessments involved in said claims for abatement, with interest, and brought actions against said Bowers in the District Court of the United States for the Southern District of New York to recover back the amounts so paid. Said actions are still pending undetermined (petitions, pp. 4, 98-9, 117, answers, pp. 15, 102, 120).

The Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, made regulations which provided that all materials carried in inventories should be valued on the basis of (*a*) *cost, or* (*b*) *cost or market value, whichever was lower,* with the presumption that the materials in the inventory were those last purchased. *The basis upon which the plaintiffs and their domestic affiliated corporations kept their accounts and made their returns for 1917 was not in accordance with said regulations* (petitions, pp. 5, 100, 118, answers, pp. 15, 102, 120). *The Commissioner ruled and determined that the basis upon which the plaintiffs and their domestic affiliated corporations valued their inventories of tin plate and determined their net incomes for 1917 did not clearly reflect their incomes and was not authorized or permitted by the Revenue Act of 1917 or the regulations made thereunder, that their incomes for 1917 should not be determined upon the basis upon which they kept their accounts and made their returns and that their income and excess profits taxes for 1917 should not be computed upon their incomes as returned. The Commissioner ruled and determined that the basis upon which the plaintiffs and their domestic affiliated*

corporations kept their accounts and made their returns for 1917 did not clearly reflect their incomes (petitions, pp. 5, 100, 118-9, answers, pp. 15, 102, 120, findings, pp. 87, 108, 126).

The net income of the American Can Company for 1917, determined upon the basis and in the manner provided in Section 12 of the Revenue Act of 1917, was $12,754,886.02 ($60,010.50 thereof being dividends upon the stock of other domestic corporations). The net income of the Missouri Can Company for 1917, determined upon such basis was $124,164.87. The net income of the Detroit Can Company for 1917, determined upon such basis was $6,556.48. The consolidated net income of the American Can Company and its domestic affiliated corporations for 1917, determined upon such basis was $13,231,054.52 ($60,010.50 thereof being dividends upon the stock of other domestic corporations) (findings, pp. 87-90, 108, 126-7, evidence, pp. 35-9, 43-6, 59-64, 66-7).

The total amount of the Federal income taxes for 1917 payable by the American Can Company upon $12,754,886.02 of net income ($60,010.50 thereof being dividends upon the stock of other domestic corporations) and of the Federal excess profits tax for 1917 payable by the American Can Company and its domestic affiliated corporations upon $13,231,054.52 of consolidated net income ($60,010.50 thereof being dividends upon the stock of other domestic corporations) was $2,514,478.94 (findings, p. 90, evidence, pp. 46, 67).

The amount of the Federal income taxes for 1917 payable by the Missouri Can Company upon $124,164.87 of net income was $7,449.87 (findings, p. 108, evidence, pp. 40, 66).

The amount of the Federal income taxes for 1917 payable by the Detroit Can Company upon $6,556.48 of net income was $393.39 (findings, p. 126, evidence, pp. 40, 66).

No part of the amounts which the plaintiffs, or any of them, paid, or which Edwards collected, as and for Federal taxes for 1917 has been refunded or repaid or credited against any income, war profits or excess profits tax or instalment

thereof due or payable by the plaintiffs, or any of them (findings, pp. 90, 109, 126-7, evidence, pp. 40-1).

The conclusions of law found by the District Court were that the plaintiffs had paid and that Edwards, as Collector of Internal Revenue, had collected from the plaintiffs, $2,705,501.71 in the case of the American Can Company, $7,763.65 in the case of the Missouri Can Company, and $5,893.80 in the case of the Detroit Can Company, in excess of the amounts which were legally payable and collectible as and for Federal income and excess profits taxes for 1917, that said amounts were assessed and collected erroneously, illegally, wrongfully and without authority and that the plaintiffs were entitled to judgments for said amounts with interest at the rate of 6% per annum from the dates of payment (pp. 90, 109, 127).

The defendant refers to the evidence which shows how the plaintiffs handled on their books the matter of valuing their normal stocks of tin plate at a constant figure (R. pp. 48-9), but this evidence tends merely to confirm the evidence previously given with respect to the basis upon which the plaintiffs kept their accounts (R. pp. 32-3). The purpose and effect of the bookkeeping entries which the plaintiffs made in January 1917 was to carry their normal stocks of tin plate at a constant figure.

It may be noted here that these bookkeeping entries were made three months before the United States declared war upon Germany (April 7, 1917), and eight months before the Revenue Act of 1917 was passed (October 3, 1917). They were made at a time when the income taxes amounted to only two per cent of the net income. Nobody had any reason to expect that the rate of the income taxes would be materially increased and the matter of income taxation had not become a matter of any great practical importance to business corporations.

It could not be claimed that the plaintiffs were seeking to avoid the payment of income taxes and it is obvious that their only purpose was to meet the violent fluctuations in

prices which had been caused by the European War. The plaintiffs acted in entire good faith and upon sound business judgment, which the Courts will not question and which in fact the defendant has never questioned (see opening statements of counsel, R. pp. 25-30).

In any case the undoubted fact is that the plaintiffs made the basis of valuing their normal stocks of tin plate at a constant figure an integral and fundamental part of their system of accounting, the system which they actually employed in their business, upon the results of which profits or losses were determined, dividends were paid, reports to the stockholders were made and the continuance of the management was decided upon. That their action was prudent and wise from a business point of view cannot be questioned, even though the basis which they used for their own business purposes could not be used for income tax purposes.

That the Commissioner actually rejected the basis used by the plaintiffs is shown by the fact that he revalued the inventories and redetermined the incomes upon a different basis and that he actually made rulings and determinations to the effect that the basis used by the plaintiffs did not clearly reflect their incomes or comply with the Regulations and that such basis could not be used for income tax purposes.

We submit that the questions presented in these cases are not stated correctly on pages 2 and 3 of the defendant's brief.

The grounds for the claims for refund which the plaintiffs filed are not stated correctly on pages 6 to 7 of the defendant's brief (R. pp. 4, 15, 99, 102, 117, 120).

Questions Open to Review.

The question whether the rulings of the District Court upon the defendant's motion for judgment and requests for findings of fact are reviewable in this Court is not of much practical importance because there was no error in any such rulings. The findings of fact are fully supported by the evidence and in exact accordance with the evidence. The facts which the defendant requested the Court to find and which the Court did not find were either not supported by the evidence or wholly immaterial or adequately covered by the facts which were found.

It is well settled that in actions brought under the Tucker Act, now Section 24, paragraph 20 of the Judicial Code, the only question that can be reviewed by an Appellate Court is the question whether the facts found are sufficient to support the judgment. The Act requires the Court to make special findings of fact and precludes the Court from making a general finding (24 Stat. 505*c*, 359, Sec. 7. Annotated Code Sec. 764). The findings of fact made by the Court are conclusive and the question whether they are supported by the evidence is not reviewable.

Chase v. *United States*, 155 U. S. 489;
United States v. *Buffalo Pitts Co.*, 234 U. S. 228.

The only apparent exception is in cases where the findings of fact purport to include a statement of all the evidence upon which the finding of some ultimate fact is based. In such cases the findings of fact present on their face the question whether the ultimate fact is supported by any evidence. The cases at bar are not exceptions to the general rule above stated.

United States v. *Clark*, 96 U. S. 37, 40;
Stone v. *United States*, 164 U. S. 380;
Collier v. *United States*, 173 U. S. 79.

The rule may be different in other actions brought in the District Court where the parties waive a jury by stipulation.

In such a case the Court may make either special findings or a general finding. The case of *Maryland Casualty Company* v. *Jones,* 279 U. S. 792, was a case of this character.

It is clear in any case that the rulings in question cannot be reviewed unless they were made in the progress of the trial of the cause and are duly presented by a bill of exceptions (R. S. Sec. 700). The docket entries show that the defendant's requests for findings of fact and motions for judgment were filed on June 11, 1927, after the Court had rendered a memorandum decision which was filed on May 31, 1927, that the first order extending the term was filed on September 17, 1927, and the bill of exceptions was filed on November 9, 1927 (R. pp. 1, 96, 114).

Rule 6 of the District Court provides that the terms of the Court at Trenton commence on the third Tuesday in January and the second Tuesday in September. The cases at bar were tried at Trenton. The second Tuesday in September, 1927, was September 13th. It thus appears that the order extending the term was not filed until after the expiration of the term.

It cannot be said that the rulings in question were made in the progress of the trial of the cause, and in any case it is obvious that they are not duly presented by a bill of exceptions.

Muller v. *Ehlers,* 91 U. S. 249;
United States v. *Jones,* 149 U. S. 262;
Michigan Insurance Bank v. *Eldred,* 143 U. S. 293;
O'Connell v. *United States,* 253 U. S. 142;
Exporters v. *Butterworth-Judson Co.,* 258 U. S. 365.

The only rulings which the District Court made in the progress of the trial of the cause were with respect to the admission or exclusion of evidence. The defendant, however, does not rely upon any of these rulings or claim that any one of them was reversible error. As a matter of fact they did not relate to the competency of the evidence or the method of proof. None of these rulings, of course, are reviewable unless they were excepted to at the time and are duly presented by a bill of exceptions.

SUMMARY OF ARGUMENT.

We will argue:

1. The Revenue Act of 1917 provided that the income of every corporation should be determined upon the basis prescribed in Section 12 of the Act, except in cases where a corporation kept its accounts and made its return upon some other basis which clearly reflected its income and complied with the Regulations made by the Commissioner with the approval of the Secretary of the Treasury.

2. The plaintiffs did not keep their accounts or make their returns for 1917 upon a basis which clearly reflected their incomes and complied with the Regulations made by the Commissioner with the approval of the Secretary of the Treasury.

3. The findings of fact established the net incomes of the plaintiffs upon the basis prescribed in Section 12 of the Revenue Act and are fully supported by the evidence.

4. The plaintiffs are entitled to judgments for the amounts of the taxes paid in excess of the amounts payable upon the cash basis, with interest at the rate of six per cent per annum from the dates of payment to a date preceding the date of the refund check by not more than thirty days, such date to be determined by the Commissioner of Internal Revenue.

POINT I.

The Revenue Act of 1917 provided that the income of every corporation should be determined upon the basis prescribed in Section 12 of the Act, except in cases where a corporation kept its accounts and made its return upon some other basis which clearly reflected its income and complied with the regulations made by the Commissioner with the approval of the Secretary of the Treasury.

The Acts of Congress which imposed and determined the amounts of the Federal income and excess profits taxes for 1917 were the Revenue Act approved September 8, 1916 (39 Stat. 756, c. 463), and the Revenue Act approved October 3, 1917 (40 Stat. 300, c. 63). These two Acts, taken together, constitute the Revenue Act of 1917. The Act of October 3, 1917, continued some of the provisions of the Act of September 8, 1916, amended some of its provisions and added some new provisions. The Revenue Acts of 1909, 1913 and 1916 imposed only taxes based upon the amount of the income. The Act of 1917 increased the rates of the income tax and added an excess profits tax based upon the amount of the invested capital and the amount of the income.

There is no doubt that the Revenue Act of 1917 prescribes the basis of actual receipts and disbursements, or the "cash" basis, as the primary basis for determining the amount of the income subject to the income and excess profits taxes. This basis is prescribed and defined in the Act with respect to both individuals and corporations. No other basis for determining income is prescribed or defined in the Act.

The only provisions of the Revenue Act of 1917 which authorize the computation of taxes upon any amounts other than the incomes determined on the cash basis, are Sections

8(*g*) and 13(*d*). The language of these two sections is exactly the same, except that the former applies to individuals and the latter to corporations.

These sections, 8(*g*) and 13(*d*), appeared for the first time in the Revenue Act of 1916. The Revenue Acts of 1909 and 1913 prescribed the cash basis for determining the amount of the income and did not authorize or permit taxpayers to make their returns upon any other basis.

The purpose of these new sections was to enable taxpayers who kept books upon bases other than the cash basis to make returns upon the basis of their books in cases where that basis clearly reflected the income, and to relieve such taxpayers from the burden of redetermining their incomes upon the cash basis. Their purpose was to grant a privilege to the taxpayers rather than to confer additional powers upon the Commissioner. These sections did not *require* any taxpayer to do anything.

Section 10 of Title 1 of the Revenue Act of 1917 imposes an income tax "upon the total net income *received* * * * by every corporation".

Section 201 of Title II of the Revenue Act of 1917 imposes an excess profits tax upon the income of every corporation, and Section 206 of the same Title provides that "for the purposes of this Title the net income of a corporation shall be *ascertained* and *returned* * * * for the taxable year upon the same basis and in the same manner as provided in Title I" of the Revenue Act of 1917.

Section 12 of Title I of the Revenue Act of 1917, so far as is material, reads as follows:

> "Section 12(*a*). In the case of a corporation, joint-stock company or association, or insurance company, organized in the United States, such net income shall be ascertained by deducting from *the gross amount of its income received within the year* from all sources—
>
> First. All the ordinary and necessary expenses *paid within the year* in the maintenance and operation of its business and properties, including rentals or other payments required to be made as a condition to the con-

tinued use or possession of property to which the corporation has not taken or is not taking title, or in which it has no equity.

Second. All losses *actually sustained and charged off within the year* and not compensated by insurance or otherwise, including a reasonable allowance for the exhaustion, wear and tear of property arising out of its use or employment in the business or trade; * * *

Third. The amount of interest *paid within the year* on its indebtedness (except on indebtedness incurred for the purchase of obligations or securities the interest upon which is exempt from taxation as income under this title) to an amount of such indebtedness not in excess of the sum of (*a*) the entire amount of the paid-up capital stock outstanding at the close of the year, or, if no capital stock, the entire amount of capital employed in the business at the close of the year, and (*b*) one-half of its interest-bearing indebtedness then outstanding. * * *

Fourth. Taxes *paid within the year* imposed by the authority of the United States (except income and excess profits taxes), or of its Territories, or possessions, or any foreign country, or by the authority of any State, county, school district, or municipality, or other taxing subdivision of any State, not including those assessed against local benefits."

There is no doubt that the basis for determining the net income which is prescribed in Section 12 is the basis of actual receipts and disbursements, or the "cash" basis.

Section 13(*a*) of Title I provides that "the tax shall be computed upon the net income, *as thus ascertained,* received within each preceding calendar year", etc., obviously referring to the basis for ascertaining net income which is prescribed in Section 12.

Section 13(*b*) of Title I provides that "every corporation * * * subject to the tax herein imposed shall, on or before the first day of March, * * * render a true and accurate return of its annual net income in the manner and form to be prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, and

containing such facts, data and information as are appropriate and, in the opinion of the Commissioner, necessary to determine the correctness of the net income returned and to carry out the provisions of this title".

Section 13(*d*) of Title I reads as follows:

> "(*d*) A corporation, joint-stock company or association, or insurance company, keeping accounts *upon any* basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect *its* income, *may,* subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make *its* return *upon* the basis *upon* which *its* accounts are kept, *in which case,* the tax shall be computed upon *its* income *as so returned.*"

There is no doubt that the basis of actual receipts and disbursements referred to in Section 13(d) is the basis for determining the net income which is prescribed in Section 12.

Section 14(*a*) of Title I provides that "all assessments shall be made and the several corporations * * * shall be notified of the amounts for which they are respectively liable on or before the first day of June of each successive year, and said assessment shall be paid on or before the fifteenth day of June * * * except in cases of refusal or neglect to make a return and in cases of *erroneous,* false or fraudulent returns, in which cases the Commissioner of Internal Revenue *shall,* upon the discovery thereof, at any time within three years after said return is due, *make a return* upon information obtained as provided for in this title or by existing law; and the assessment made by the Commissioner of Internal Revenue *thereon* shall be paid by such corporation * * * immediately upon notification of the amount of such assessment; * * *"

Section 14(*b*) of Title I provides that "When the assessment shall be made, as provided in this title, the returns, together with any corrections thereof which may have been made by the commissioner, shall be filed in the office of the Commissioner of Internal Revenue".

Section 13, including all its subdivisions, appears in the

Revenue Act under the heading "Returns", and Section 14, including all its subdivisions, appears in the Revenue Act under the heading "Assessment and Administration". It cannot be presumed that provisions of this character are intended to impose a tax or to affect in any way the substantive provisions of the Act which do impose the tax.

Reinecke v. *Gardner*, 277 U. S. 239, 242-4.

Sections 13(*b*), 14(*a*) and 14(*b*) are purely administrative and they do not affect or qualify in any way the substantive provisions of the Act with respect to the determination of the income and the computation of the tax. These sections do not authorize the Commissioner to make an additional assessment or to make a "correction" of a return unless he makes a new return. The procedure clearly outlined in cases where no return is made or an erroneous return is made, is for the Commissioner to obtain the necessary information and make the return which the Revenue Act *required* the corporation to make, and to make an additional assessment "thereon". The "corrections" of returns to which reference is made in Section 14(*b*) include only the "corrections" which the Commissioner is authorized to make by making new returns.

It is clear beyond question that in making a return and determining the amount of the income to be stated therein, the Commissioner is bound to follow the substantive provisions of the Act with respect to the determination of the income. There are no provisions in the Act with respect to the determination of the income other than those to which we have already referred.

Section 13(*d*) qualifies Section 12 and Section 13(*a*) to the extent, and only to the extent, that it is inconsistent with them, and it withdraws from Section 12 and Section 13(*a*) those cases, and only those cases, which fall clearly within its terms. Section 12 and 13(*a*) state the general rule. Section 13(*d*) creates an exception. All cases which do not fall clearly within the terms of an exception are necessarily gov-

erned by the general rule, and all cases which do not fall clearly within the terms of Section 13(*d*) are necessarily governed by Section 12 and Section 13(*a*).

The only cases which fall within the terms of Section 13(*d*) are cases where a corporation keeps its accounts and makes its return upon a basis which clearly reflects its income and complies with the Regulations, made by the Commissioner, with the approval of the Secretary of the Treasury. In a case where a corporation does not so keep its accounts *and* make its return, Section 13(*d*) does not apply and the tax should be computed upon the cash basis prescribed in Section 12.

It is clear that Section 13(*d*) did not *authorize* any corporation to make a return upon any basis other than the cash basis, unless it complied with the Regulations made by the Commissioner, with the approval of the Secretary of the Treasury, and clear that one function of such Regulations was to prescribe rules for determining whether the basis used by any particular corporation was one which clearly reflected its income and one which the corporation had the right to use for income tax purposes under Section 13(*d*). In every case where a corporation made a return upon a basis other than the cash basis it was the duty of the Commissioner to determine whether the basis used by the corporation was one which clearly reflected its income, and obviously the intention of Congress that he should do so under general rules so that all taxpayers would have fair and equal treatment.

The Regulations which the Commissioner made, with the approval of the Secretary of the Treasury, were conclusive upon the question whether any particular basis other than the cash basis was one which clearly reflected the income and could be used for income tax purposes under Section 13(*d*).

It is equally clear that Section 13(*d*) did not *require* any corporation to make a return upon any basis other than the cash basis. Section 13(*d*) merely *authorized* a corporation to make a return upon a basis other than the cash basis, if

it was able to comply, and did comply, with that Section and with the Regulations. Section 13(*d*) did not *require* any corporation to do anything.

There is no reason for placing any forced or unnatural interpretation upon the language of Section 13(*d*), and if there were any doubt as to its meaning the doubt should be resolved in favor of the plaintiffs rather than the defendant.

In the first place Section 13(*d*) appears in a Revenue Act and it is well settled that all provisions of a Revenue Act should be construed strictly against the Government and in favor of the taxpayer; in the second place Section 13(*d*) is an exception which qualifies Sections 12 and 13(*a*), and it is well settled that an exception in a statute should be construed strictly so as not to take out of the general clause any case which does not fall clearly within the terms of the exception; and in the third place Section 13(*d*) is a new provision which had no counterpart in the Revenue Acts before 1916 and it is well settled that a new provision of law should be construed strictly so as not to change the existing law any more than is clearly indicated by the terms of the new provision.

The authorities establish the general rule that the Commissioner has no power to compute or assess taxes unless it affirmatively conferred by an Act of Congress by clear and unequivocal language. Revenue Acts are not to be extended, by implication, beyond the clear import of the language used. In case of doubt they are to be construed most strongly against the Government and in favor of the taxpayer. An omission in a Revenue Act cannot be supplied by the courts or the Commissioner.

Gould v. *Gould*, 245 U. S. 151;
United States v. *Field*, 255 U. S. 257;
Smietanka v. *First Trust & Savings Bank*, 257 U. S. 602;
United States v. *Merriam*, 263 U. S. 179.
Iselin v. *United States*, 270 U. S. 245;
Reinecke v. *Gardner*, 277 U. S. 239, 244.

The authorities also establish "the general rule of law which has always prevailed, and become consecrated almost as a maxim in the interpretation of statutes, that where the enacting clause is general in its language and objects, and a proviso is afterwards introduced, that proviso is construed strictly, and takes no case out of the enacting clause which does not fall fairly within its terms. In short, a proviso carves special exceptions only out of the enacting clause; and those who set up any such exception, must establish it as being within the words as well as within the reason thereof."

United States v. *Dickson,* 15 Peters 141, p. 165;
Ryan v. *Carter,* 93 U. S. 78, p. 83;
Schlemmer v. *Buffalo, Rochester, etc., Railway,* 205 U. S. 1.

The authorities also establish the general rule that when Congress adopts a new provision of law, it is not presumed that Congress intends to change the existing law any further than is clearly indicated by the terms of the new provision. The cases refer frequently to the familiar rule that "in construing altered revenue laws, the whole system must be regarded in each alteration, and no disturbance allowed of existing legislative rules of general application beyond the clear intention of Congress".

Steamship Company v. *Joliffe,* 2 Wallace 450;
Shaw v. *Railroad Co.,* 101 U. S. 557, 565;
Bear Lake Irrigation Company v. *Garland,* 164 U. S. 1;
Johnson v. *Southern Pacific Co.,* 196 U. S. 1, 17;
Maul v. *U. S.,* 274 U. S. 501;
Quinn v. *Bancroft-Jones Corp.,* 18 Fed. 2nd 727, 728 (C. C. A., 2nd Cir. 1927);
Gillam v. *U. S.,* 27 Fed. 2nd 296 (C. C. A. 4th Circ. 1928).

The authorities also establish the general rule that an act of Congress should be interpreted in accordance with the

language used by Congress, and that such language should be interpreted in accordance with its natural and ordinary meaning, Congress being presumed to know the meaning of words and rules of grammar. "No mere omission, no mere failure to provide for contingencies, which it may seem wise to have been specifically provided for, justify any judicial addition to the language of the statute." Ordinarily there is no excuse for departing from a literal interpretation of the language used by Congress.

United States v. *Goldenberg,* 168 U. S. 95;
Ozawa v. *United States,* 260 U. S. 178;
Lewellyn v. *Harbison,* 31 Fed. 2nd 740 (C. C. A. 3rd Cir., 1929);
Van Camp & Sons Co. v. *American Can Co.,* 278 U. S. 245.

In the case last cited, the Supreme Court said at page 147:

> "Decisions of this court, where the letter of the statute was not deemed controlling and the legislative intent was determined by a consideration of circumstances apart from the plain language used, are of rare occurrence and exceptional character, and deal with provisions which, literally applied, offend the moral sense, involve injustice, oppression or absurdity (*United States* v. *Goldenberg,* 168 U. S. 95, 103, 42 L. ed. 394, 398, 18 Sup. Ct. Rep. 3), or lead to an unreasonable result, plainly at variance with the policy of the statute as a whole (*Ozawa* v. *United States,* 260 U. S. 178, 194, 67 L. ed. 199, 207, 43 Sup. Ct. Rep. 65)."

In *United States* v. *Anderson,* 269 U. S. 422, this Court had occasion to consider Sections 10, 12(*a*), 13(*a*) and 13(*d*) in connection with adjustments which the Commissioner made with respect to the taxes for 1916 and 1917, resulting in a net increase of the tax for 1917. The corporations involved in this case kept their accounts on the basis of accruing all their receipts and disbursements and they accrued on their books in 1916 their munitions taxes for 1916, which were payable and paid in 1917. They made their

returns for 1916 and 1917 on the basis of their books except that they deducted their munitions taxes from their incomes for 1917 instead of their incomes for 1916. The Commissioner ruled that their munitions taxes should be deducted from their incomes for 1916 instead of their incomes for 1917, and this Court sustained the adjustment of the taxes made in accordance with this ruling.

The corporations admitted that the basis on which their accounts were kept clearly reflected their incomes and that they were not able to make their returns on the basis of actual receipts and disbursements and they made no effort to prove the amounts of their incomes on the basis of actual receipts and disbursements.

The Government contended that the corporations had elected to make their returns on the accrual basis and that accordingly the Commissioner had the right to redetermine their incomes on the accrual basis. The corporations contended that they had the right under the Revenue Act to deduct their taxes in the year in which they were paid, and that in any case taxes did not accrue until they were due and payable. This Court did not sustain any one of these contentions but, on the contrary, held that as the corporations were not able to make their returns on the basis of actual receipts and disbursements, and as their accounts were kept on a basis which clearly reflected their incomes and complied with the Regulations, they were required to make their returns on the basis of their own books of account, and that the adjustments made by the Commissioner merely had the effect of making their returns accord with their own books of account.

Mr. Justice Stone, in writing the opinion of the Court, said at pages 436 *et seq.* (Italics ours):

> "While § 12(*a*) taken by itself would appear to require the income tax return to be made on the basis of actual receipts and disbursements, it is to be read with § 13(*d*) which we have quoted and which *obviously limits in some respects the operation of* § 12(*a*) by providing in substance that a corporation keeping its books

on a basis other than receipts and disbursements, *may make its return on that basis provided it is one which reflects income.*

"Standing by themselves and taken at their face value, these sections would seem to *require* the taxpayer to make its return on the basis of receipts and disbursements or, in the alternative, *on the basis of its own books of account if they reflect true income,* under such regulations as the Commissioner may make, and indeed to *require* the latter alternative *if the taxpayer is unable to make a return except on that basis.*

"So interpreting the statute, the Commissioner, with the approval of the Secretary of the Treasury, on January 8, 1917, before appellee made its income tax return for 1916, promulgated Treasury Decision 2433 which provides in part that under § 13(*d*) it 'will be permissible for corporations which accrue on their books monthly or at other stated periods amounts sufficient to meet fixed annual or other charges to deduct from their gross income the amounts so accrued, provided such accruals approximate as nearly as possible the actual liabilities for which the accruals are made, and provided that in cases wherein deductions are made on the accrual basis as hereinbefore indicated, income from fixed and determinable sources accruing to the corporations must be returned, for the purpose of the tax, on the same basis.' It also provided in substance that when the taxpayer, following a consistent accounting practice sets up reserves to meet liabilities, the 'amount of which or date of maturity' is not definitely determinable, such reserve may be deducted from gross income. The decision also laid down a procedure for readjusting such reserves when the amount actually required for that purpose was definitely ascertained, and *provided that if returns upon this basis of 'accrual or reserve' did not reflect true net income, the taxpayer would not be permitted to make its return on any other basis than that of 'actual receipts and disbursements'.*

"We think that the statute was correctly interpreted by the Commissioner and that his decision referred to was consistent with its purpose and intent.

At page 439:

"But, in the Act of 1916, Congress added § 13(*d*), *which did not have its counterpart in earlier legislation.*

This section went further than any previous regulation by *authorizing* the tax return to be made on the basis on which the taxpayer's books were kept, *provided only that the basis was one reflecting income and the return complied with regulations made by the Commissioner.*

"Treasury Decision 2433, to which reference has been made, was in harmony with this view of § 13(*d*). It recognized the right of the corporation to deduct all accruals and reserves, without distinction, *made on its books* to meet liabilities, provided the *return* included income accrued and, *as made,* reflected true net income. If the *return* failed so to reflect income, the regulation reserved the right of the Commissioner *to require the return to be made on the basis of receipts and disbursements.*"

At page 440:

"The taxpayer *being unable to make its return on a strict receipts and disbursements basis, and not having attempted to do so,* could not have complied with § 13(*d*) and Treasury Decision 2433 by deducting either accruals of interest or expenses alone without the other, or without deducting other *reserves made on its books* to meet liabilities such as the munitions tax, incurred in the process of creating income."

At page 443:

"Since the suit was one to recover a tax erroneously exacted, *the burden was on the petitioners,* appellees here, *to prove the facts establishing the invalidity of the tax.* But the findings fail to show affirmatively that the books were kept or the return made on the basis of receipts and disbursements. Indeed, the facts found, to which we have referred, show that the books were kept on the basis of accruals and reserves to meet liabilities incurred. It does not appear that there was any expense or liability of the taxpayer incurred by its operations during the year which was not *accrued on its books.* Its return was made on that basis, but omitted munitions taxes *accrued on its books during the year* for which the return was made."

In *Reinecke* v. *Gardner,* 277 U. S. 239, it was held that the Revenue Act of 1917 did not require a trustee in bankruptcy

to pay the excess profits tax, although it did require him to pay the income tax, and it was further held that the question whether the taxpayer should deduct interest accrued in 1916 but paid in 1917 from his gross income for 1916 or his gross income for 1917 could not be answered, because the record did not show whether the books of the taxpayer "as kept" reflected his income, and did not show on what basis his return was made. The record did show that the taxpayer was carrying on the business of a coal mining corporation and keeping his books upon an accrual basis. The Court held in substance that the taxpayer was required to make his return upon the cash basis, unless he kept his books on an accrual basis which accurately reflected his income, and actually made his return on that basis. The Court said at pages 244-5 (Italics ours):

> "The applicable section, 13(*d*) of the Act of 1916, directs that if the taxpayer keeps his books on any basis other than that of actual receipts and disbursements, and the return is made on the basis adopted, the tax shall be computed on that basis *unless the books clearly do not reflect the taxpayer's true income.* In *United States* v. *Anderson,* 269 U. S. 422, it was pointed out that under the Act of 1916 and applicable treasury regulations, *the taxpayer must make all deductions from gross income as of the year when the payments were made unless he keeps his books on an accrual basis which accurately reflects his income, and actually made his return on that basis.* See *United States* v. *Mitchell,* 271 U. S. 9; *American National Co.* v. *United States,* 274 U. S. 99. The present certificate fails to state whether the books of the trustee *as kept* reflected his income or whether his return was made on the accrual basis or on the basis of actual receipts and disbursements. Under Jud. Code, § 239 the facts pertinent to the question asked must be certified. When they are omitted from the certificate the question need not be answered. *Dilton* v. *Strathearn S. S. Co.,* 248 U. S. 182."

These two decisions sustain the proposition that if the basis upon which the accounts are kept, or the return is made, does not clearly reflect the income or does not comply with

the Regulations, the tax should be computed upon the cash basis.

They also sustain the proposition that if the books "as kept," or the return "as made," do not clearly reflect the income or do not comply with the Regulations, the tax should be computed upon the cash basis.

In the *Anderson* case the taxpayers kept their accounts upon a basis which clearly reflected their incomes and complied with the Regulations, and they were not able to make their returns upon the cash basis. In that case the only basis which could be used was the book basis.

In the cases at bar the plaintiffs did not keep their accounts upon a basis which clearly reflected their incomes and complied with the Regulations, and they were able to make their returns upon the cash basis. In these cases the only basis which could be used is the cash basis.

There is no reason why the taxes of the plaintiffs should not be computed in strict accordance with the Revenue Act.

The defendant contends in substance that if a corporation used a basis or made a return which did not clearly reflect the income or did not comply with the Regulations, the Commissioner had the power to redetermine the income and compute the tax upon the basis prescribed in the Regulations.

This contention is refuted not only by the language of the Revenue Act of 1917 and the two decisions last above mentioned, but also by the changes which Congress made in the Revenue Acts for 1918 and subsequent years with respect to the determination of the income. The provisions of these Acts with respect to the determination of the income are entirely different from those of the prior Acts.

Section 233(*a*) of the Revenue Act of 1918 provides that in the case of a corporation the term "gross income" means the gross income as defined in Section 213, with certain exceptions applicable to insurance companies. Section 213 provides that the term "gross income" includes "gains, profits and income derived from * * * trades, businesses, commerce, or sales, or dealings in property," etc. and that "The

amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, *unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period".*

Section 234(*a*) provides that in computing the net income of a corporation there shall be allowed as deductions "(1) All the ordinary and necessary expenses *paid or incurred* during the taxable year in carrying on any trade or business," etc., "(2) all interest *paid or accrued* within the taxable year on its indebtedness," etc., "(3) taxes *paid or accrued* within the taxable year," etc. and certain other amounts representing losses, depreciation, amortization, etc.

The last paragraph of Section 200 provides:

> "The term 'paid,' for the purposes of the deductions and credits under this title, means 'paid or accrued' or 'paid or incurred,' and the terms 'paid or incurred' and 'paid or accrued' shall be construed according to the method of accounting upon the basis of which the net income is compiled under section 212."

Subdivision (*b*) of Section 212, an entirely new and most important provision, is as follows:

> "(*b*) The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) *in accordance with the method of accounting regularly employed in keeping the books of such taxpayer;* but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made *upon such basis and in such manner as in the opinion of the Commissioner does clearly reflect the income."*

The Revenue Acts prior to 1918 made no reference to inventories. The Revenue Act of 1918, however, provides in Section 203:

> "That whenever in the opinion of the Commissioner the use of inventories is necessary in order clearly to

determine the income of any taxpayer, inventories shall be taken by such taxpayer upon such basis as the Commissioner, with the approval of the Secretary, may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income."

The later Revenue Acts contained substantially the same provisions with respect to the determination of the income and the powers of the Commissioner in connection therewith.

Revenue Act of 1921, approved Nov. 23, 1921, 42 Stat. 227 c. 136, Secs. 233(*a*), 213, 234(*a*), 200(4), 212(*b*), 203.

Revenue Act of 1924, approved June 2, 1924, 43 Stat. 253 c. 234, Secs. 233(*a*) 213, 234(*a*), 200(*d*), 212(*b*), 205.

Revenue Act of 1926, approved Feb. 26, 1926, 44 Stat. 9 c. 27, Secs. 233(*a*), 213, 234(*a*), 200(*d*), 212(*b*), 205.

Revenue Act of 1928, approved May 29, 1928, 45 Stat. 791, c. 852, Secs. 21, 22(*a*), 23, 48(*c*), 41, 22(*c*).

The fact that the Revenue Acts for 1918 and subsequent years conferred upon the Commissioner the power to prescribe a basis for determining the income, and to redetermine the income on such basis, in cases where the basis used by a taxpayer did not clearly reflect his income, by provisions entirely different from any contained in the prior Acts, tends strongly to show that the Commissioner had no such power under the prior Acts.

U. S. v. *Field,* 255 U. S. 257;

Smietanka v. *First Trust & Savings Bank,* 257 U. S. 602;

Shwab v. *Doyle,* 258 U. S. 529 (1922).

POINT II.

The plaintiffs did not keep their accounts or make their returns for 1917 upon a basis which clearly reflected their incomes and complied with the Regulations made by the Commissioner with the approval of the Secretary of the Treasury.

The Regulations which the Commissioner issued under the Revenue Acts of 1916 and 1917, with the approval of the Secretary of the Treasury (Reg. 33 revsd.) included the following:

> "Art. 91. Manufacturing corporations.—Gross income for the purpose of returns of manufacturing companies shall consist of the total sales plus the inventory at the end of the year less the sum of the cost of goods or materials purchased during the year and the inventory at the beginning of the year. Instructions as to how inventories shall be taken will be included in special regulations to be furnished upon application to the Collector of Internal Revenue."

Special Regulations with respect to the valuation of inventories were issued by the Commissioner, with the approval of the Secretary of the Treasury, in the form of a letter to Collectors of Internal Revenue dated December 19, 1917 (T. D. 2609). They included the following:

> "Inventories of supplies, raw materials, work in process of production, and unsold merchandise, must be taken either (a) at cost, or (b) at cost or market price, whichever is lower."

It is obvious that these Regulations applied only to the matter of determining the income of a manufacturing corporation upon an accrual basis. They had no relation to the matter of determining the income upon the cash basis pre-

scribed in Section 12. Neither the "sales" made by a corporation, nor the "cost" of goods or materials purchased by a corporation, nor the "inventory" of a corporation at the beginning or the end of the year is an actual receipt or an actual disbursement. These factors are not mentioned in Section 12 and they can be used only in connection with an accrual basis of accounting for income. (See Point III, *infra.*)

The Regulations above mentioned are undoubtedly valid for the purpose of determining whether an accrual basis used by a manufacturing corporation was one which clearly reflected its income and one which the corporation had the right to use for income tax purposes under Section 13(*d*).

These Regulations establish conclusively that no manufacturing corporation could make a return under Section 13(*d*) unless it accrued its receipts and disbursements, and used inventories valued upon the basis of (a) cost, or (b) cost or market price, whichever was lower, reflecting in its income the difference between the inventory at the beginning of the year and the inventory at the end of the year. They establish conclusively for income tax purposes that no other basis would clearly reflect the income of such a corporation. This is conceded and asserted throughout the defendant's brief (pp. 20, 22, 27-8, 32-3).

The Commissioner did not issue any Regulations with respect to the valuation of inventories prior to December 19, 1917. The Regulations which he then issued precluded the use for income tax purposes of the basis upon which the plaintiffs had already kept their accounts during 1917 and made it impossible for the plaintiffs to make returns for 1917 under Section 13(*d*). No corporation had the right to make a return under that Section unless it kept its accounts upon a basis which clearly reflected its income and complied with the Regulations.

The purpose and effect of inventories when used in connection with an accrual basis of accounting for income is clearly shown in two rulings which the Commissioner issued in the latter part of 1919 (T. B. R. 48, 1 Cum. Bul. 47, T. B. R. 65, 1 Cum. Bul. 51). In these rulings the Advisory

Tax Board considered carefully the question whether certain bases for valuing inventories, other than the bases of (a) cost, and (b) cost or market price whichever is lower, were bases which clearly reflected the income and should be authorized by the Regulations for income tax purposes. These other bases included the basis used by the plaintiffs, which is sometimes called the "base stock" method. The Advisory Tax Board reached the conclusion that no one of these other bases would clearly reflect the income assignable to an annual accounting period, that no one of them was authorized, and no one of them should be authorized, by the Regulations for income tax purposes.

In T. B. R. 48 the Advisory Tax Board said:

> "Request has been made for advice as to whether the average cost method of taking inventories used by certain corporations is permissible under the act of September 8, 1916, or under the act of October 3, 1917. Briefly stated, the method in question is as follows:
>
> "Materials purchased during a month are added, both as to quantity and cost, to the quantity and cost balance brought forward from the previous month, and an average cost to the close of the month is computed by dividing the total quantity into the total money figures. This average is then applied to the quantity of materials used for manufacture during the month, and the amount so computed is credited to the material account. This process is a well-established custom, which has been adopted by the leading concerns of the trade.
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> * * * * * *
>
> "Commercial practice sanctions the custom of an annual accounting for profits or losses, and the income tax laws have required such annual accounting. It must be admitted, however, that such a computation is not only difficult, but that a year is in many businesses a period too short to be satisfactory. * * * Whatever the difficulty and whatever the degree of accuracy in attaining it, the object to be kept in view is the ascertainment of the profits during the year which have been realized upon sales actually made, inasmuch as profits can arise only through the sale or exchange of property. * * * The

logical method of computation is, therefore, to apply against the total sales of the period the cost of the goods covered by such sales, and the difference between these two amounts represents gross profits. Precisely this is accomplished when inventories are taken upon the basis of cost.

"A loss, although seemingly the opposite of a profit, may, however, fall under a different rule. A loss may be occasioned by physical destruction or deterioration of property included in an inventory or it may be attributable to changes in styles or other causes affecting salability, or it may be occasioned by shrinkage in market value. Where such losses arise, even though not fully consummated by a sale of the goods, the fact should nevertheless be recognized, and when such goods are taken in an inventory they may, if the taxpayer so elects as a consistent policy, be valued at market instead of cost, where market is lower. This is true even in spite of the possibility that conditions may change, and at a date before a sale is made the goods may again be worth their original cost. * * * The rule of cost or market, whichever is lower, even though it may appear to lack in consistency, thus, nevertheless, rests upon solid ground, and its widespread adoption throughout the business world amply justified its adoption for tax purposes.

* * * In a business requiring goods to be carried for lengthy periods and where an average method of inventory valuation is used, this overstatement of profits will occur whenever the current market is declining, while on an advancing market the profits on the actual sales of the year will be understated. When the market is stable the average method will reflect with approximate accuracy the true profits, and in a business in which the turnover is rapid the effect of such a method upon the computation of annual income is small as compared with a business in which it is necessary to carry goods, such as raw materials, for long periods. * * * The computation of net income upon such a basis results in an assignment of income to a year, not upon the basis of the transactions of the year, but upon the basis of transactions part of which spread over more than a year. * * * An annual accounting period is a fundamental requirement of the Federal income-tax legislation, and every computation of taxable net income must

be made in conformity therewith. This the average cost inventory method failed to do, and its use can not be approved as meeting the statutory requirement."

In T. B. R. 65 the Advisory Tax Board said (Italics ours):

"The question is raised as to whether under the Revenue Acts of 1917 and 1918 the so-called 'base stock,' 'minimum,' or 'cushion,' hereinafter referred to as 'base stock,' method of taking inventories may be used.

"Section 203 of the Revenue Act of 1918 provides as follows:

"That whenever in the opinion of the Commissioner the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer upon such basis as the Commissioner, with the approval of the Secretary, may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income.

"Article 1582 of Regulations 45 provides in part that:

"Inventories should be valued at (a) cost, or (b) cost or market, whichever is lower.

"*According to the base-stock method of taking inventories a manufacturer or dealer values at the same price year after year the minimum quantity of goods which he must have on hand at all times.*

* * * * * *

"Clearly the base-stock method of taking inventories is not within the terms of the regulations—that is, it is not such a basis as the Commissioner, with the approval of the Secretary, has prescribed. It remains to consider, however, whether such a method should be so prescribed 'as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income.'

"The facts before the Advisory Tax Board do not warrant the conclusion that there has been any general adoption of the base-stock method of taking inventories as an 'accounting practice,' or that it has had any considerable recognition as the 'best' accounting practice.

On the contrary, it is certain that the method has not been widely adopted. * * * In particular, the fact that so few business concerns use the base-stock method is strongly suggestive of the truth that *it does not truly reflect the income.*

"That it is a truth appears as clearly upon analysis as upon an examination of trade practice. The present Federal income-tax system is based upon an annual accounting period. *The object of an inventory is to assign to an annual accounting period its profits and losses. The effect of the base-stock inventory method is to assign all profits and losses in respect of the minimum inventory to the year in which such inventory is liquidated.* This result is accomplished through ignoring sales and exchanges of individual items of the inventory and treating the minimum inventory as a unit. Each sale or exchange of property for other property having a market value is, however, in fact a realization of taxable profit or deductible loss in the year in which it occurs and *a method of accounting which disregards such realization does not truly reflect income.*

* * * * * *

"Where the base-stock method is used it is true, as was stated in Advisory Tax Board Recommendation 48 with respect to the average cost inventory method that 'in a business requiring goods to be carried for lengthy periods * * * *this overstatement of profits will occur whenever the current market is declining, while on an advancing market the profits on the actual sales of the year will be understated.'* The Advisory Tax Board, therefore, concludes that *the base-stock inventory method does not 'most clearly' reflect income.* For a more complete discussion of the subject of inventories see the Advisory Tax Board recommendation above referred to.

* * * * * *

"It is suggested in behalf of the taxpayer that if the base-stock method is not approved, some alternative method should be prescribed other than the valuation of inventories as required by the present regulations at cost or market, whichever is lower. One method proposed is that inventories be valued on a moving average basis over a period of five years, more or less. According to this method one-fifth, for example, of the inventory

would be deemed to be the goods most recently purchased, and the balance the goods on hand at the beginning of the year. Another method proposed is that the goods in the inventory be deemed to be the earliest rather than the latest purchases. *These methods are open to the same objections as is the base stock method. Inventories valued according to these methods would not as clearly reflect the income assignable to an accounting period as do inventories valued according to the present regulations.*

"Most of the reasoning above set forth with respect to the Revenue Act of 1918 applies to the Revenue Act of 1917. The Advisory Tax Board finds nothing in the earlier statute to warrant the use thereunder of methods of valuing inventories which can not be used under the later statute.

"The Advisory Tax Board is of opinion, therefore, that neither the base stock method of taking inventories nor the moving average method, nor a method based upon the presumption that goods in the inventory are the earliest purchases, is in conformity with the provisions of the Revenue Act of 1917 or of the Revenue Act of 1918, and recommends that no change be made in the present regulations with respect to the method of taking inventories."

These rulings show clearly, and indeed it is quite obvious as a matter of law, that (1) the word "basis" as used in Section 13(*d*) means a basis of accounting for, and determining the amount of, the net income of a corporation for a taxable year, (2) a basis which clearly reflects the income means a basis which measures accurately the amount of the true net income of a corporation for a taxable year, (3) the purpose of using inventories is to assign the net income of a corporation to separate accounting periods and determine the amount of the net income separately for each accounting period, (4) each one of the various different bases for valuing inventories affects differently the assignment of the net income to separate years and the determination of the amount of the net income for each year, and (5) an accrual basis of accounting does not clearly reflect the income

and comply with the Regulations unless it includes the use of inventories valued upon a basis which clearly reflects the income and complies with the Regulations.

The difference between one basis for valuing inventories and another basis for valuing them is similar in kind to the difference between the cash basis and any accrual basis. The difference in either case is with respect to the assignment of the net income to separate accounting periods and the time as of which the net income is deemed to be earned.

It is obvious that although the average cost method and the base stock method for valuing inventories cannot be used for income tax purposes, they are proper and desirable methods for business corporations to use. These methods reflect the true net income approximately over a period of years, and they tend to stabilize the income from year to year and lessen the effect thereon of fluctuations in prices. The life of a corporation is not limited to one year and it is proper for any corporation to so conduct its business as to preserve a reasonable equilibrium and stability over a period of years, particularly at a time of abnormal price conditions.

While the base stock method is not used so generally as the cost or market method, it is used by many business corporations, including such well known corporations as the American Smelting & Refining Company and the National Lead Company. It was used by the Chicago Frog & Switch Company whose case was decided by the Court of Claims June 3, 1929 (Unofficially reported in Federal Courts Volume of Corporation Trust Company's Tax Service C. L. 67108) and the Western Dry Goods Company whose case was decided by the District Court for the Western District of Washington July 3, 1929 (Unofficially reported in District Courts Volume of Corporation Trust Company's Tax Service, p. 8180). These cases are cited on page 25 of the defendant's brief.

The defendant's brief admits that the plaintiffs are entitled to have their taxes computed upon the cash basis and to recover any excess which they may have paid over the amounts legally payable upon that basis, if the basis upon

which they kept their accounts and made their returns did not clearly reflect their incomes (pp. 28-30), that the basis upon which the plaintiffs valued their inventories and determined their incomes, both in keeping their accounts and making their returns, did not clearly reflect their incomes and did not comply with the Regulations, and that the Commissioner revalued their inventories and redetermined their incomes upon a different basis, *i. e.,* the basis prescribed in the Regulations (pp. 5-6, 10, 20, 22, 26, 27, 28, 33).

The defendant argues however that the word "basis" as used in Section 13(*d*) does not mean a basis for determining the income of a corporation for a taxable year, that it has reference only to two fundamental systems of accounting generally known as "the cash basis" and "the accrual basis", that when Section 13(*d*) referred to "any basis other than that of actual receipts and disbursements", it referred to "an equally basic system of accounting", meaning "the accrual basis", that the matter of valuing inventories has no bearing upon the treatment of items of income and expenditures and nothing to do with the basis of accounting as that term is used in Section 13(*d*), that the plaintiffs kept their accounts and made their returns upon "the accrual basis", that the Commissioner had power to redetermine their incomes upon "the accrual basis" in accordance with the Regulations and that the changes made by the Commissioner corrected the errors in the returns "without disturbing the basic accrual system of accounting, so that it is entirely clear that the accrual system as corrected discloses respondents' true net income" (pp. 21-3, 26-28).

One obvious difficulty with this argument is that an accrual basis does not clearly reflect the income and comply with the Regulations unless it includes the use of inventories valued upon a basis which clearly reflects the income and complies with the Regulations.

The mere statement that the plaintiffs kept their accounts and made their returns upon the accrual basis does not show the basis upon which they valued their inventories, and con-

sequently does not show that they kept their accounts or made their returns upon a basis which clearly reflected their incomes and complied with the Regulations.

The defendant's argument ignores the fundamental requirement of Section 13(*d*) which was that no basis could be used for income tax purposes under that Section unless it clearly reflected the income and complied with the Regulations.

The word "basis" as used in Section 13(*d*) meant something which either did or did not clearly reflect the income, and either did or did not comply with the Regulations, and it must have meant something which was complete and specific enough to enable a person to determine whether it did or did not clearly reflect the income, and whether it did or did not comply with the Regulations.

It is true that there are no bases, other than the cash basis, except those which include the accrual of receipts and disbursements, but it does not follow that there is only one accrual basis. It is obvious that an accrual basis with inventories valued upon one basis is different from an accrual basis with inventories valued upon a different basis.

Section 13(*d*) did not refer to the accrual basis or even use the word "accrual". It did not provide that if a corporation kept its accounts and made its return upon "the accrual basis" the tax should be computed upon "the accrual basis". On the contrary, it referred to "*any* basis other than that of actual receipts and disbursements", authorized a corporation which kept its accounts upon *any* such basis to make its return upon *the* basis upon which *its* accounts were kept, if such basis clearly reflected its income, and provided that if a corporation kept its accounts and made its return upon such a basis, the tax should be computed upon *its* income *as so returned.* Section 13(*d*) clearly recognized that there was more than one basis other than that of actual receipts and disbursements, and consequently recognized that there was more than one form or kind of an accrual basis and that each different form or kind of an accrual basis was a different basis of accounting for income.

When Section 13(*d*) referred to the basis of actual receipts and disbursements, it referred to the basis or method for determining net income which is prescribed in Section 12, and when it referred to any basis other than that of actual receipts and disbursements, it must have referred to any basis or method for determining the net income other than that prescribed in Section 12.

Section 13(*d*) did not authorize the Commissioner to redetermine the income of a corporation upon the basis prescribed in the Regulations. It merely authorized him in certain cases to compute the tax upon the income "as so returned." These words cannot mean anything other than (*a*) the amount of the income stated in the return or (*b*) the amount of the income determined upon the basis upon which the corporation kept its accounts and made its return, *i. e.,* the basis upon which the corporation determined its income when it kept its accounts and made its return.

If a corporation kept its accounts and made its return upon an accrual basis with inventories, it is obvious that nobody could determine the income of the corporation upon the basis used by the corporation unless he knew and used the basis upon which the corporation valued its inventories.

The correct interpretation of Section 13(*d*) is clearly indicated by the language of this Court in *Reinecke* v. *Gardner,* where it said that the tax should be computed upon the cash basis unless the taxpayer "keeps his books on *an accrual basis which accurately reflects his income,* and actually made his return on that basis". The question is not whether the corporation kept its accounts and made its return upon *an* accrual basis or upon *the* accrual basis, but whether it kept its accounts and made its return upon a form or kind of an accrual basis which accurately reflected its income.

While the matter of valuing the inventories is separate and distinct from the treatment of items of receipts and disbursements, it does have some relation to the treatment thereof, for the reason that it is not feasible to use inventories at all unless the receipts and disbursements are accrued. To add or subtract the value of inventories to or from actual

receipts or actual disbursements would be wholly incongruous and the result would be wholly unintelligible.

If inventories are used in connection with any basis of accounting, the basis upon which they are valued affects the assignment of the net income to separate accounting periods, and the amount of the net income for each period, and affects the time as of which the net income is deemed to be earned. A change in the basis for valuing the inventories is just as much a change in the basis of accounting as a change in the basis for treating the receipts and disbursements.

The defendant's statement that the Commissioner did not disturb "the *basic* accrual system of accounting" and that "the accrual system *as corrected* [by the Commissioner] discloses respondents' true net income" (p. 28) demonstrates the fallacy which underlies the defendant's entire argument. Inasmuch as the Commissioner did disturb the valuation of the inventories, it is obvious that the system which the defendant calls the "basic accrual system" does not include the use or valuation of inventories. Inasmuch as the Commissioner did correct the valuation of the inventories, it is obvious that the system which the defendant calls the "accrual system" does include the use and valuation of inventories. The defendant's statement shows that the system which reflects the true net income is "the accrual system as corrected" by the Commissioner, and not the "basic accrual system" or the "accrual system" as used by the plaintiffs. It also shows that the system which did or did not clearly reflect the income was the "accrual system" which included the use of inventories, rather than the "basic accrual system" which did not include the use of inventories.

The system of accounting which the plaintiffs used included both the accrual of receipts and disbursements and the valuation of inventories. The matter of valuing the inventories was just as much a part, and just as essential a part, of the system as the matter of accruing receipts and disbursements. Neither part could be changed without changing the system of accounting. If either part failed to clearly reflect the income and comply with the Regulations,

it is obvious that the system failed to clearly reflect the income and comply with the Regulations.

The Circuit Court of Appeals for the Third Circuit held that the basis used by the plaintiffs did not reflect their true net incomes, because of the fact that they valued their inventories at a constant figure, regardless of cost or market value, that the "change by the Commissioner was not the mere or incidental change or correction of a figure in a system, but the change of a system, from one basis to a different basis", and that since the basis used by the plaintiffs did not reflect their true net income, the only basis which could be used under the Revenue Act was the cash basis prescribed in Section 12 (R. pp. 134-5).

There was no occasion for any specific finding to the effect that the basis upon which the plaintiffs kept their accounts and made their returns did not clearly reflect their incomes, because the facts which are established by the pleadings and the findings show conclusively that the basis used by the plaintiffs could not be used for income tax purposes under Section 13(*d*).

The findings show that the plaintiffs kept their accounts during 1917 upon the basis of accruing their receipts and disbursements, *and using inventories valued at a constant figure, regardless of cost or market value* (R. pp. 86, 107, 126), that the plaintiffs determined their incomes and made their returns for 1917 upon the basis upon which their accounts were kept and that the amount of the consolidated net income as so determined and returned was $17,994,400.46 including dividends (R. pp. 87, 107, 126).

The above facts were established by undisputed evidence, which was admitted without objection or exception taken by the defendant (R. pp. 33-5) and were conceded by the findings which the defendant requested the District Court to make (R. pp. 83, 104, 122). The defendant does not question any one of the above findings and apparently concedes that they were all supported by the evidence.

The pleadings and the findings show that the Commissioner objected to the basis upon which the plaintiffs valued

their inventories and determined their incomes and *revalued their inventories* and *redetermined their incomes upon a different basis,* and that the consolidated net income as so redetermined was $24,949,668.51 including dividends (R. pp. 3-4, 15, 98, 102, 117, 120), and that *the basis upon which the plaintiffs kept their accounts and made their returns for 1917 was not in accordance with the Regulations* which the Commissioner made, with the approval of the Secretary of the Treasury, *with respect to the valuation of inventories* (R. pp. 5, 15, 100, 102, 118, 120).

The above facts were conceded by the answers and also by the findings which the defendant requested the District Court to make (R. pp. 84, 85, 104, 105-6, 123, 124).

The pleadings and the findings thus show conclusively that the basis used by the plaintiffs did not clearly reflect the income and comply with the Regulations and could not be used for income tax purposes under Section 13(*d*).

The pleadings and the findings show in addition the rulings and determinations which the Commissioner made to the effect that the basis used by the plaintiffs did not clearly reflect their incomes or comply with the Regulations and that their incomes should not be determined upon such basis (R. pp. 5-6, 15, 100, 102, 118, 120, 84, 85, 104, 105-6, 123, 124). They show these rulings and determinations not as a conclusion of law or as a conclusion from other facts alleged or found, but as independent and separate facts. There is no warrant for the claim that the allegations or findings with respect to these rulings and determinations involved an interpretation of the letters of March 7, 1921 which the Commissioner wrote to the plaintiffs. The inference is that the Commissioner made his rulings and determinations before he wrote the letters. There is no ground to infer that he made them only by the letters. The plaintiffs did not offer any evidence with respect to these rulings and determinations because there was no occasion for them to prove allegations of the petitions which were admitted by the answers.

These rulings and determinations were made by the Com-

missioner in the performance of his duties and within the scope of his authority under the Revenue Act. Any such ruling or determination by an administrative officer is binding and conclusive upon the Government, unless it is impeached by the Government for fraud or other adequate cause.

U. S. v. *Kaufman*, 96 U. S. 567;
U. S. v. *Savings Bank*, 104 U. S. 728;
Steel v. *Smelting Co.*, 106 U. S. 447;
Lee v. *Johnson*, 116 U. S. 48;
Heath v. *Wallace*, 138 U. S. 573;
U. S. v. *California & Oregon Land Co.*, 148 U. S. 31;
Bates v. *Payne*, 194 U. S. 106;
Houston v. *Packing Co.*, 249 U. S. 479.

The defendant has made no attempt to impeach the rulings and determinations which the Commissioner made in the cases of these plaintiffs. The defendant does not even contend that they were erroneous or improper. The fact that the Commissioner made these rulings and determinations shows conclusively as a matter of law that the basis used by the plaintiffs could not be used for income tax purposes under Section 13(*d*).

It is well settled that findings of fact are sufficient to support a judgment if the facts found, together with such inferences as may properly be drawn therefrom, are sufficient to show that the judgment was correct. Even when a material fact is omitted, the judgment will be affirmed if such fact appears sufficiently from the other facts which are found.

United States v. *Pugh*, 99 U. S. 265;
Sun Mutual Ins. Co. v. *Ocean Ins. Co.*, 107 U. S. 485;
The Belgenland, 114 U. S. 355;
United States v. *California & Oregon Land Co.*, 148 U. S. 31;
Winton v. *Amos*, 255 U. S. 373.

We submit that the opinion of the Circuit Court of Appeals for the Second Circuit in *American Can Company* v.

Bowers wholly fails to meet the issues. This opinion does not recognize or meet the contentions which the plaintiffs actually made, although it undertakes to refute a number of contentions which the plaintiffs did not make. We contend that it does not interpret correctly either the facts or the law, and does not recognize the real purpose or effect of inventories. It does not undertake to interpret the word "basis" as used in Section 13(*d*) or to define the basis upon which the plaintiffs kept their accounts and made their returns, or to determine whether the basis used by the plaintiffs was one which clearly reflected their incomes. It holds in substance that the Commissioner had the power to redetermine the incomes in accordance with the Regulations, although it does not point to any provision of the Revenue Act which conferred any such power.

We have never argued or claimed that there is no occasion for reconciliation of the net profits of the plaintiffs as per their books with their Federal tax returns for 1917, or that the Commissioner was required under the law to compute their taxes upon their incomes as returned by them without correction. The contentions which we made in the New York cases are entirely consistent with those made in the cases at bar.

It is obvious that the report of the Ways and Means Committee of the House, referred to on page 23 of the defendant's brief, can have no bearing upon the interpretation of the Revenue Act of 1917 as it was finally enacted.

United States v. *Trans-Missouri Freight Assn.*, 166 U. S. 290, 318;
Standard Oil Co. v. *U. S.*, 221 U. S. 1, 50.

The quotation from the opinion of this Court in *United States* v. *Mitchell*, 271 U. S. 9, which is printed on page 24 of the defendant's brief, has nothing to do with the Revenue Act of 1917. That case arose under the Revenue Act of 1918 and this Court did not undertake in that case to say anything about the Revenue Act of 1917.

The case of *Vang* v. *Lewellyn*, 35 Fed. 2nd, 283, which is cited on page 24, and the cases cited on page 25, of the defendant's brief, were entirely different from the cases at bar. The taxpayers did not contend in any of those cases that their taxes should be computed upon the cash basis or even offer to prove the amounts of their incomes upon the cash basis. They contended on the contrary that their returns were correct as made. They did not prove that the taxes which they had paid were in excess of the taxes which were legally payable. There is nothing in any of these cases to throw any doubt upon the judgments in the cases at bar.

Treasury Decision 2433, to which the defendant refers at the bottom of page 25 of its brief, tends to confirm rather than question the contentions made by the plaintiffs. This decision merely provided that it would be *"permissible"* for corporations to make returns under Section 13(*d*) upon an accrual basis, provided that they made returns which clearly reflected their incomes, and used the same basis consistently year after year, and that if any corporation failed to so make its return it would not be permitted to make its return upon any basis other than the cash basis.

Treasury Decision No. 2609, referred to on page 4 of the defendant's brief, also tends to confirm the plaintiff's contentions, particularly the proviso at the end of paragraph A. The requirement that the method adopted for the valuation of inventories must be adhered to in subsequent years clearly shows that a change in the method for valuing the inventories would involve a change in the basis of accounting for the income.

POINT III.

The findings of fact established the net incomes of the plaintiffs upon the basis prescribed in Section 12 of the Revenue Act and are fully supported by the evidence.

The defendant does not point out or suggest that there is any defect in the findings of the District Court with respect to the incomes of the plaintiffs upon the cash basis. The defendant contends merely that the findings are not supported by the evidence because the evidence shows that the incomes upon the cash basis were not determined in accordance with Article 91 of Regulations 33 revised, *i. e.*, by the use of "sales", "purchases" and "inventories". The defendant does not, however, contend that the incomes of the plaintiffs upon the cash basis were not determined in accordance with Section 12 of the Revenue Act. It will be noted that the defendant's brief does not even make any reference to this section.

Section 12 requires and permits the use of only five factors in determining the amount of the net income (1) the gross amount of the income *received within the year,* (2) the amount of the ordinary and necessary expenses of maintenance and operation *paid within the year,* (3) the amount of the losses actually *sustained and charged off within the year,* (4) the amount of the interest on indebtedness *paid within the year,* and (5) the amount of the taxes *paid within the year.* The net income is ascertained under this Section by deducting the last four factors from the first factor.

The findings and the evidence show separately for each Company, and in the aggregate for all the Companies, the amount of each one of these five factors and that each factor includes the items and only the items which are included in the definition of the factor contained in Section 12. There is no ground for claiming that the amounts given for gross

income fail to include any item which ought to have been included or that the amounts given for the deductions include any item which ought not to have been included. The findings and the evidence show also the amount of the net income of each Company and the consolidated net income of all the Companies upon the cash basis prescribed in Section 12 (R. pp. 87-90, 108, 126-7, 35-9, 43-6, 59-64, 66-67).

When the plaintiffs offered in evidence their computation of their incomes upon the cash basis, the defendant asked for an opportunity to examine the books and records of the plaintiffs with a view to checking the correctness of their computation. The plaintiffs did not oppose this application and the Court adjourned the trial for several weeks in order to allow the defendant to check the computation. When the trial was resumed the defendant conceded the figures in the plaintiffs' computation, except for two items which the plaintiffs corrected. (R. pp. 38-40, 43-5).

The figures shown in the findings of fact are in exact accordance with the figures shown in the plaintiffs' computation as corrected to meet the objections of the defendant. The plaintiffs' computation was supported by the testimony of their chief accounting officer and the concessions of the defendant.

There is no warrant for the claim that it is necessary to comply with Article 91 of the Regulations or to compute the cost of goods sold in order to determine the net income of a corporation upon the basis prescribed in Section 12, for the simple reason that Section 12 does not require or permit the use of such factors as "sales," "cost," "purchases" or "inventories." These factors can be used only in connection with an accrual basis of accounting.

Article 91 of the Regulations is in conflict with Section 12 and cannot have the effect of changing the statute.

It is not possible to use accounts receivable, accounts payable or inventories in connection with the basis of actual receipts and disbursements because they are neither actual receipts nor actual disbursements.

The defendant's argument that Article 91 applies to the cash basis as well as an accrual basis would lead to the result that the income of a corporation upon the cash basis is the same as its income upon an accrual basis, which is palpably absurd.

It is well settled that when the income is determined upon the cash basis no items should be used or taken into consideration other than items of cash actually received within the year, items of cash actually paid within the year and losses actually sustained within the year.

Maryland Casualty Co. v. *U. S.*, 251 U. S. 342;
U. S. v. *Anderson*, 269 U. S. 422;
United States v. *Mitchell*, 271 U. S. 9;
Mutual Benefit Ins. Co. v. *Herold*, 198 Fed. Rep. 199 (D. C. N. J. 1912); 201 Fed. Rep. 918 (C. C. A. 3rd Cir.);
Connecticut General Life Insurance Co. v. *Eaton*, and *Connecticut Mutual Insurance Co.* v. *Eaton*, 218 Fed. Rep. 188, 206 (D. C. Conn.); affirmed on appeal, 223 Fed. Rep. 1022 (C. C. A. 2nd Cir.);
Edwards v. *Keith*, 231 Fed. Rep. 110 (C. C. A. 2nd Cir.);
U. S. v. *Christine Oil & Gas Co.*, 269 Fed. Rep. 458 (D. C. La.);
Lumber Mutual Fire Insurance Co. v. *Malley*, 256 Fed. Rep. 380 (D. C. Mass.);
Coley v. *Pickering*, 21 Fed. 2nd 247 (Dist. Ct. S. D. Ill.) 1927;
American Can Co. v. *Bowers*, (D. C. N. Y.) (Petition for certiorari p. 36);
Aluminum Castings Co. v. *Routzahn*, 24 Fed. 2nd 230 (D. C. Ohio); 31 Fed. 2nd 669 (C. C. A. 6th Cir.).

It may be true that the cash basis prescribed in Section 12 does not reflect the "true net income" of a manufacturing corporation, as was indicated by this Court in *United States*

v. *Anderson,* 269 U. S. 422, and *American National Company* v. *United States,* 274 U. S. 99, but the important point is that Congress did not levy the taxes for 1917 upon the "true net income" of corporations, leaving to the Commissioner or the Regulations the matter of determining the true net income. On the contrary, it levied the taxes for 1917 upon the incomes of corporations determined upon the basis prescribed in Section 12, except in cases which fell within the terms of Section 13(*d*). It does not make any difference whether the basis prescribed in Section 12 is one which reflects the "true net income". The Commissioner has no power to assess any tax unless he does so in accordance with the Revenue Act.

When Congress prescribed the cash basis for income tax purposes it probably considered that the cash basis would be the simplest and easiest basis for the great majority of taxpayers to use and for the Government agents to check. This is particularly true with respect to the multitude of small shopkeepers and tradesmen throughout the country, whether incorporated or not, who do not have their accounts kept or certified by skilled accountants. The matter of accruing receipts and disbursements and valuing inventories involves to some extent questions of opinion and judgment with respect to which different business men may honestly differ, while the cash basis involves only a mathematical computation. The cash basis would in the long run reflect the true net income of taxpayers just as accurately as any other basis, and inasmuch as the taxes were payable in cash it was reasonable for Congress to levy them only upon the cash income actually received.

That the use of inventories is a departure from the basis of actual receipts and disbursements was recognized in the argument of the Solicitor General in behalf of the Government in *United States* v. *Anderson,* 269 U. S. 422. It was there stated (p. 423):

> "The first corporation income tax Act of October 3, 1913, like the 1909 Act, provided for the calculation of net taxable income on the receipts and disbursements

basis. Under these two Acts some *departures* from the strict receipts and disbursements basis was permitted by the Commissioner of Internal Revenue, *such as the use of inventories* * * * The resulting system was a *mongrel* one."

That inventories are not used when income is determined on the basis of actual receipts and disbursements, has frequently been recognized by the Commissioner of Internal Revenue. In 1921 the Commissioner issued T. D. 3104 which added a new article to Regulations 45 issued under the Revenue Act of 1918. The first sentence of this article read as follows:

"Art. 1585(a). *Inventories of live-stock raisers and other farmers.* (1) Farmers may *change* the basis of their returns from that of *receipts and disbursements* to that of an *inventory* basis, which necessitates the use of opening and closing *inventories* for the year in which the change is made" (4 C. B. 52).

He later issued O. D. 841, the first sentence of which read as follows:

"It is not contemplated by Treasury Decision 3104 that farmers must obtain formal permission in order to *change* the basis of their returns from that of *receipts and disbursements* to that of an *inventory basis*" (4 C. B. 53).

He later issued O. D. 939 which reads in part as follows:

"Where a change is made by farmers in the basis of making their returns from that of *cash receipts and disbursements* to that of an *accrual basis with inventories,* many items of gross income and deductions may be duplicated or entirely omitted as a result of the change unless an adjustment is made of the net income for the prior years, * * * It is therefore not permissible for farmers *in changing to the inventory basis* of making their returns to make adjustments by calculating their net income for the current taxable year without taking as a credit the *inventory* of live stock, crops, and other products at the beginning of the year in accordance with the instructions on page 4 of Form 1040-F" (4 C. B. 54).

There is no evidence to show how the plaintiffs determined the amounts of the expenses of maintenance and operation shown in their computation or how much, if anything was included for purchases of tin plate. The fact that the plaintiffs had on hand more tin plate at the end of 1917 than at the beginning of 1917 is of no importance whatever. The evidence shows that they had on hand less tin plate at the end of 1916 than at the beginning of 1916 (R. p. 54). It is obvious that their stocks had been diminished during 1916 and natural that they should increase their stocks during 1917. However, the record shows conclusively that the amounts given for expenses included nothing other than the amounts defined in Section 12 and that they were correct.

There is nothing in *Doyle* v. *Mitchell Brothers,* 247 U. S. 179, or *Hays* v. *Gauley Mountain Coal Co.,* 247 U. S. 189, which throws any doubt upon the plaintiffs' computation of their income upon the cash basis. These cases involve only the matter of determining the income derived through the sale of *capital assets* under the Revenue Act of 1909. The Government contended that the entire proceeds of the sale of the capital assets were income and that if the taxpayers had the right to deduct anything therefrom they had the right to deduct only the original cost which was less than the market value on December 31, 1908, when the Revenue Act took effect. The taxpayers contended that they had the right to deduct the market value of the assets on December 31, 1908. This Court referred to various Regulations, some with respect to the determination of the income of a manufacturing corporation, and others with respect to the determination of the income derived through the sale of capital assets. Those which related to the capital assets were in accordance with the taxpayers' contention and this Court held that the taxpayers' contentions were correct. There is no doubt that this Court approved the Regulations which related to the capital assets, but there is no ground for saying that it approved the Regulations which related to the incomes of manufacturing corporations.

The difference between capital assets and income assets is obvious. The proceeds of the sale of capital assets are not income receipts. They do not represent income in any sense unless they include a profit. On the other hand, the proceeds of the sale of income assets, such as manufactured products, are income receipts.

It is obvious that if the net income of a corporation is determined upon an accrual basis for 1916 and upon the cash basis for 1917, receipts and disbursements which are accrued at the end of 1916 will be included in both calculations. The effect is to include in the income for each year the net income accrued at the end of the first year. This fact, however, can have no bearing upon the interpretation of Section 12 or the matter of determining the income for 1917 in accordance with that section.

POINT IV.

The plaintiffs are entitled to judgments for the amounts of the taxes paid in excess of the amounts payable upon the cash basis, with interest at the rate of six per cent per annum from the dates of payment to a date preceding the date of the refund check by not more than thirty days, such date to be determined by the Commissioner of Internal Revenue.

It is well settled that an erroneous return is not binding upon the taxpayer any more than upon the Government, and that if a taxpayer pays an amount of taxes in excess of the amount which was legally payable he has the right to recover back the excess, regardless of the reason for the overpayment, and regardless of whether it was made voluntarily or under protest or duress.

Revenue Act of 1916, 39 Stat. 756 c. 463, Sec. 14(a);

Revenue Act of 1918, 40 Stat. 1057 c. 18, Sec. 252;

Revenue Act of 1921, 42 Stat. 227 c. 136, Sec. 252;

Revenue Act of 1924, 43 Stat. 253 c. 234, Sec. 281(a), Sec. 1014;

Revenue Act of 1926, 44 Stat. 9 c. 27, Sec. 284, Sec. 1122(c);

Judicial Code, as amended Feb. 24, 1925, Sec. 24, par. 20;

U. S. v. *Hvoslef,* 237 U. S. 1;

Capewell Horse Nail Company v. *Walsh,* 1 Fed. 2nd 818 (D. C. Conn.); 4 Fed. 2nd 991 (C. C. A., 2nd Cir.);

Beatty v. *Heiner,* 10 Fed. 2nd 390 (D. C. Pa.);

Warner v. *Walsh,* 24 Fed. 2nd 449 (D. C. Conn.);

Baker & Taylor Co. v. *U. S.,* 26 Fed. 2nd 187 (C. C. A., 2nd Cir.).

After the Circuit Court of Appeals had entered judgments of affirmance, the plaintiffs moved for the amendment of the judgments so as to comply with Section 177 of the Judicial Code as amended by Section 615 of the Revenue Act of 1928, which changed the rule with respect to the allowance of interest on claims of this character and directed that a provision with respect to the allowance of interest should be included in every judgment. The Circuit Court of Appeals entered orders amending their judgments *nunc pro tunc* so as to comply with Section 177 of the Judicial Code as so amended and state the exact amounts of the overpayments of the taxes and the dates from which and to which interest thereon should be paid (R. pp. 139-142).

If this Court should affirm the judgments of the Circuit Court of Appeals as so amended, the matter of the allowance of interest would be covered. If, however, it should affirm the judgments of the District Court, we suggest that this Court should include in its judgments provisions with respect to the allowance of interest, in accordance with Section 177 of the Judicial Code as amended, so that the mandates to the District Court would include similar provisions. If this Court should merely affirm the judgments of the District Court without including such provision for interest, the District Court might be in doubt with respect to the interpretation of the mandates and consequently in doubt as to whether its judgments to be entered on the mandates should or should not include such provisions for interest.

Section 177 of the Judicial Code as amended by the Revenue Act of 1928 took effect on June 29, 1928. It included the following:

> "(b) In any judgment of any court rendered (whether against the United States, a collector or deputy collector of internal revenue, a former collector or deputy collector, or the personal representative in case of death) for any overpayment in respect of any internal-revenue tax, interest shall be allowed at the rate of 6 per centum per annum upon the amount of the overpayment, from the date of the payment or collection thereof to a date

preceding the date of the refund check by not more than thirty days, such date to be determined by the Commissioner of Internal Revenue."

The judgments of the District Court in the cases at bar ere entered on August 16, 1927. They included interest the rate of six per cent per annum from the dates of the verpayments to the dates of entry of the judgments (R. p. 91, 110, 128). This was in accordance with Section 177 the Judicial Code as amended by the Revenue Act of 1926, hich provided that interest should be allowed at the rate of x per cent per annum from the date of the overpayment the date of the entry of the judgment or if the judgment as reviewed by an Appellate Court to the date of entry of he final judgment.

The Tucker Act as amended February 13, 1925 and ncorporated in the United States Code on June 30, 1926, rovided that from the date of the final judgment or decree gainst the United States interest should be computed thereon t the rate of four per cent until the time when an appropria-ion was made for the payment of the judgment or decree 24 Stat. 507, Sec. 10; 43 Stat. 940, Sec. 8).

It is obvious that Section 177 of the Judicial Code as mended by the Revenue Act of 1928 was intended to super-ede all previous provisions with respect to interest on claims f this character and was intended to apply to all judgments endered after the amendment took effect, including judg-nents entered in the first instance by a Trial Court, judg-nents entered by an Appellate Court and judgments entered y the Trial Court upon the mandate of an Appellate Court.

Conclusion.

The only returns which the Revenue Act authorized or required the plaintiffs to make were returns upon the cash basis. The returns which the plaintiffs made were more favorable to the Government than the returns which the Revenue Act authorized and required them to make. The effect of allowing the plaintiffs to recover the taxes which they paid in excess of the taxes payable upon the cash basis, with interest from the dates of payment, is merely to put the plaintiffs in the position where they would have been if they had made, in the first instance, the returns which the Revenue Act authorized and required them to make. The inherent justice of allowing such a recovery is self evident.

Respectfully submitted,

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On the Brief.

SUPREME COURT OF THE UNITED STATES.

Nos. 128, 129, 130.—October Term, 1929.

128 The United States, Petitioner, *vs.* American Can Company.

129 The United States, Petitioner, *vs.* Missouri Can Company.

130 The United States, Petitioner, *vs.* Detroit Can Company.

On Writs of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

[February 24, 1930.]

Mr. Justice McReynolds delivered the opinion of the Court.

In the courts below these causes were heard together and one opinion here will suffice.

Respondent, The American Can Company owned the entire capital stock of respondents Missouri Can Company and Detroit Can Company. All were incorporated under the laws of New Jersey and had their legal residences and principal offices therein. Their places of business were within the Second United States Internal Revenue District of New York. William H. Edwards, formerly Collector for that District, retired March 1921; Frank K. Bowers succeeded him. During Edwards' term he demanded and collected from these three corporations income and excess profits taxes for 1917 aggregating more than $5,200,000. Thereafter Collector Bowers exacted of them above $3,300,000 as additional income and excess profits taxes for the same year.

In January, 1926, respondents instituted actions against the United States in the District Court for New Jersey, as permitted under U. S. Code, Sec. 41, Par. 20 (Judicial Code, Sec. 24, Par. 20; Revenue Act, Nov. 23, 1921, c. 136, Sec. 1310 (c), 42 Stat. 311; Revenue Act, February 24, 1925, c. 309, 43 Stat. 972). They sought

to recover with interest more than $2,700,000 paid, as they alleged, to Edwards in excess of taxes properly assessable to them for 1917. Judgments against the United States for the amounts claimed were affirmed by the Circuit Court of Appeals, Third Circuit, March 5, 1929; and the matter is here upon certiorari.

They also sued Bowers, Collector, in the District Court, Southern District of New York, to recover the additional taxes for 1917 ($3,300,000) demanded by and paid to him. These suits involved the same questions as those presented in the causes now before us. Judgments went for Bowers, Collector. The Circuit Court of Appeals, Second Circuit, affirmed them November 4, 1929.

The opinions and judgments in the two Circuits upon the same facts are thus in direct conflict.

Pertinent provisions of the statutes and Treasury Regulations are printed in the margin.*

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*The Revenue Act of September 8, 1916, Sec. 10, imposed taxes reckoned upon the amount of income.

The Act of October 3, 1917, Chap. 63, 40 Stat. 300, 302, 303, 305, increased the income tax rates; also imposed an excess profits tax. It provided—

Title I, Sec. 4. "That in addition to the tax imposed by subdivision (a) of section ten of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, there shall be levied, assessed, collected, and paid a like tax of four per centum upon the income received in the calendar year nineteen hundred and seventeen and every calendar year thereafter, by every corporation, joint-stock company or association, or insurance company, subject to the tax imposed by that subdivision of that section. . . .

"The tax imposed by this section shall be computed, levied, assessed, collected, and paid upon the same incomes and in the same manner as the tax imposed by subdivision (a) of section ten of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, except, &c. . . .

"Title II— . . .

"Sec. 201. That in addition to the taxes under existing law and under this act there shall be levied, assessed, collected, and paid for each taxable year upon the income of every corporation, partnership, or individual, a tax (hereinafter in this title referred to as the tax) equal to the following percentages of the net income: . . .

. . . .

"Sec. 206. That for the purposes of this title the net income of a corporation shall be ascertained and returned . . . (c) for the taxable year upon the same basis and in the same manner as provided in Title I of the Act entitled 'An Act to increase the revenue, and for other purposes,' approved September eighth, nineteen hundred and sixteen, as amended by this Act, except . . ."

The accounts of respondents were kept during 1917 not upon the basis of actual receipts and disbursements but upon the accrual basis—that is pecuniary obligations payable to or by the Company were treated as if discharged when incurred. Purporting to proceed as permitted by Sec. 13 (d), Title I, Revenue Act of 1916, they made returns to the Collector upon the same basis. The Commissioner ascertained that the books showed excessive inventory values and thereby indicated net incomes much too small. The valuation placed on large quantities of tin plate had been marked up from $3.60 per box to $7.00, and the higher rather than the lower cost of this raw material had been reported. Thereupon, he disallowed the inflation, corrected the erroneous entries and made reassessments according to the returns so modified. Respondents claimed that this action amounted to rejection of the basis upon which their returns had been made. Also, that, after such rejection, no assessment could be made except one based upon receipts and disbursements; that is, upon amounts ascertained by deduct-

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The Act of September 8, 1916, 39 Stat. 756, 765, 766, 767, 770, 771, Chap. 463, provided—

Title I, Sec. 10. "That there shall be levied, assessed, collected, and paid annually upon the total net income received in the preceding calendar year from all sources by every corporation, joint-stock company or association, or insurance company, organized in the United States, no matter how created or organized but not including partnerships, a tax of two per centum upon such income; . . .

"Sec. 12 (a). In the case of a corporation, joint-stock company or association, or insurance company, organized in the United States, such net income shall be ascertained by deducting from the gross amount of its income received within the year from all sources" [Expenses, losses, interest, taxes.]

"Sec. 13 (a). The tax shall be computed upon the net income, as thus ascertained, received within each preceding calendar year ending December thirty-first: . . .

"(b) Every corporation, joint-stock company or association, or insurance company, subject to the tax herein imposed, shall, on or before the first day of March, nineteen hundred and seventeen, . . . render a true and accurate return of its annual net income in the manner and form to be prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, and containing such facts, data, and information as are appropriate and in the opinion of the commissioner necessary to determine the correctness of the net income returned and to carry out the provisions of this title. The return shall be sworn to by the president, vice-president, or other principal officer, and by the treasurer or assistant treasurer. The return shall be made to the collector of the district in which is located the principal office

ing from gross income received, expenses paid out, losses charged off, interest, and taxes (Sec. 12, Act 1916). And further, that computation should be made without regard to inventories.

The District Court for New Jersey and the Circuit Court of Appeals, Third Circuit, accepting respondents' view, awarded and approved judgments against the United States aggregating some four million dollars. The result, we think, is manifestly erroneous. Upon the findings, judgments should have gone the other way.

The claims of respondents rest upon improper construction of Par. (d), Sec. 13, Act of Sept. 8, 1916. This provides that "a corporation . . . keeping accounts upon any basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect its income, may, subject to regulations . . . make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned; . . ."

"Basis of keeping accounts" as there used refers to the general bookkeeping system followed by the taxpayer and not to the accuracy or propriety of mere individual items or entries upon the

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of the corporation, company, or association, where are kept its books of account and other data from which the return is prepared, . . .

. . . .

"(d). A corporation, joint-stock company or association, or insurance company, keeping accounts upon any basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect its income, may, subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned; . . ."

Treasury Decision No. 2609, promulgated December 19, 1917—

"(1). For the purposes of income and excess-profits tax returns, inventories of merchandise, etc., and of securities will be subject to the following rules:

"A. Inventories of supplies, raw materials, work in process of production, and unsold merchandise must be taken either (a) at cost or (b) at cost or market price, whichever is lower, provided that the method adopted must be adhered to in subsequent years, unless another be authorized by the Commissioner of Internal Revenue.

. . . .

"C. Gain or loss resulting from the sale or disposition of assets inventories as above must be computed as the difference between the inventory value and the price or value at which sold or disposed of.

"(2). In all other cases inventories must be taken at cost or at value as of March 1, 1913, as the case may be."

books. And to correct an improper item in a return—whether the result of mere error or designed—cannot properly be said to constitute rejection of the basis upon which the return was constructed. The statute empowers tax officers to make necessary rules and regulations and to take action essential to orderly enforcement of the obligations imposed. Here, the taxpayers kept their accounts on the accrual basis and elected to make their returns accordingly. They cannot complain because an item therein was changed so as to conform with admitted facts. If their returns had been made on the basis of actual receipts and disbursements certainly they would have been subject to correction for errors without changing the basis; and the same thing is true of returns framed upon an accrual basis.

United States v. *Anderson*, 269 U. S. 422, 437, 440, 443, considered the meaning of Sec. 12 (a) and 13 (d), Act of 1916, and sustained the action of the Commissioner who had reassessed according to an adjusted return originally made up on the accrual basis.

We need not discuss the question whether under any circumstances the taxable income of a manufacturing or mercantile corporation can be ascertained without reference to inventory values. Certainly, in most instances, where the taxpayer carries on an extensive business this cannot be done.

The challenged judgments are reversed. The causes will be remanded to the District Court for appropriate action in harmony with this opinion.

Reversed.

A true copy.

Test:

Clerk, Supreme Court, U. S.